

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

PENN AMERICA GROUP INC
Form 10-K/A
November 12, 2002

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K/A

FOR ANNUAL AND TRANSITION REPORTS
PURSUANT TO SECTIONS 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2001

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file Number 022316

PENN-AMERICA GROUP, INC.
(Exact Name of Registrant as Specified in Its Charter)

Pennsylvania 23-2731409
(State or Other Jurisdiction of (I.R.S. Employer
Incorporation or Organization) Identification No.)

420 S. York Road, Hatboro, PA 19040
(Address of Principal Executive Offices) (Zip Code)

Registrant's telephone number, including area code (215) 443-3600

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
<u>Common stock, par value, per share</u>	<u>New York</u>

Securities registered pursuant to Section 12(g) of the Act:

None
(Title of class)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No _____.

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Form 10-K.

As of March 22, 2002, the aggregate market value of the outstanding Common Stock held by non-affiliates of the Registrant was approximately \$69,149,535. As of March 22, 2002, there were 11,546,204 shares of the Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE:

Portions of the Registrant's definitive Proxy Statement with respect to the Registrant's 2002 Annual Meeting of Shareholders, to be filed not later than 120 days after the close of the Registrant's fiscal year, are incorporated by reference in Part III of this report.

PENN-AMERICA GROUP, INC.
ANNUAL REPORT ON FORM 10-K/A
DECEMBER 31, 2001

	Page
PART I	
ITEM 1. BUSINESS.....	3
ITEM 2. PROPERTIES.....	19
ITEM 3. LEGAL PROCEEDINGS.....	19
ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY-HOLDERS.....	19
PART II	
ITEM 5. MARKET FOR REGISTRANT'S COMMON STOCK AND RELATED STOCKHOLDER MATTERS.....	20
ITEM 6. SELECTED FINANCIAL DATA.....	21
ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.....	22
ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.....	35
ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.....	38
ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.....	61
PART III	
ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT.....	62
ITEM 11. EXECUTIVE COMPENSATION.....	62
ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.....	62
ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.....	62

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

ITEM 14. CONTROLS AND PROCEDURES.....63

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND
REPORTS ON FORM 8-K.....64

Page 2

PART I

Explanatory Note

Penn-America Group, Inc. ("PAGI" or the "Company") has recently resolved various accounting and disclosure comments from the Securities and Exchange Commission ("SEC"), in conjunction with the Company's registration statement filing relating to the issuance of additional shares of common stock. One of the comments addressed the timing of recording other-than-temporary ("OTT") declines in the market value of certain equity securities. In order to resolve the comments, the Company agreed to amend its accounting policy and record OTT write-downs on these securities for the periods ending December 31, 2001, 2000 and 1999. This restatement affects net income for each of these periods but has no affect on stockholders' equity since the unrealized loss on these securities was already recorded in Accumulated Other Income (Loss) in the Consolidated Balance Sheets and Statements of Stockholders' Equity. The Company has restated its financial statements for the affected periods and has filed such restatements on this amended Form 10-K for the year ended December 31, 2001. For further information, see Note 1 of the Notes to Consolidated Financial Statements.

In addition, the SEC staff requested that PAGI add certain disclosures or not report certain items. Business, Selected Financial Data, the Consolidated Financial Statements and Managements' Discussion and Analysis of Financial Condition and Results of Operations, included herein, have been amended as appropriate to respond to these requests.

The filing of this amended Form 10-K shall not be deemed an admission that the original filing, when made, included any untrue statement of a material fact or omitted to state a material fact necessary to make a statement not misleading.

ITEM 1. BUSINESS

General

Penn-America Group, Inc. ("PAGI") is a specialty property and casualty insurance holding company which, through its subsidiary, Penn-America Insurance Company ("Penn-America") and its subsidiary, Penn-Star Insurance Company ("Penn-Star") (collectively the "Company"), markets and underwrites commercial property, general liability and multi-peril insurance for small businesses located primarily in small towns and suburban and rural areas. Penn-America writes business in all fifty states and the District of Columbia. The Company writes business on both an admitted and non-admitted (excess and surplus lines) basis in thirty-six states, on only an admitted basis in two states and on only a non-admitted basis in twelve states and the District of Columbia. The Company chooses in each state whether to write business on an admitted or non-admitted basis based upon the Company's analysis of competition in each state. Writing business on an admitted basis is highly regulated. The regulations, which vary by state, generally govern licensing, underwriting rules, rates and policy forms, and require insurance companies to pay premium taxes and guaranty fund assessments. Writing business on a non-admitted basis is significantly less

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

regulated and provides much more freedom in setting rules, rates and policy forms and removes insurance companies from premium taxes and guaranty fund assessment liabilities. Coverage written on a non-admitted basis is less comprehensive than coverage issued on an admitted basis. If the Company chooses non-admitted status, the Company could be at a competitive disadvantage to carriers writing on an admitted basis if those competitors choose to offer coverages which are more comprehensive and attractive to an insured. Further, surplus lines agents are prohibited from writing nonadmitted business in states in which they are not resident. Thus, if the Company does not have resident surplus lines agents in every state (currently, we do not in 7 states), the Company is precluded from writing business on a non-admitted basis in those states.

Page 3

Penn-America Insurance Company was formed in 1975 by Irvin Saltzman, Chairman of the Board of Directors, who began working in the insurance industry in 1947 when he founded a general agency. The Company completed an initial public offering ("IPO") on October 28, 1993, at a price of \$4.00 per share, which was then followed by a secondary offering in July of 1997 where 4,537,500 shares were sold by the Company for net proceeds of approximately \$9.67 per share. Currently, the Saltzman family, substantially through their ownership of Penn Independent Corporation ("Penn-Independent"), owns approximately 40% of the Company's Common Stock. Jon S. Saltzman, Irvin Saltzman's son, is a Director, President and Chief Executive Officer of the Company and has been employed by the Company since 1986. Prior to 1986, Jon Saltzman was employed by Penn Independent from 1976 to 1986.

Marketing and Distribution

Penn-America's commercial insureds consist primarily of small, "Main Street" businesses including restaurants, mercantiles and non-residential service contractors. In addition, the Company has developed customized products and coverages for other small commercial insureds such as daycare facilities, fitness centers and special events. The Company believes it has benefited from a general migration of small businesses out of urban centers and into suburban and rural areas. Industry consolidation, corporate downsizing and the increased use of communications technology and personal computers, among other factors, have contributed to the high growth in the number of small businesses in these areas. The Company selects only insurance lines of business and industry segments for which it reasonably can estimate future loss costs and the resulting price levels needed to produce a satisfactory return to the Company. Therefore, the Company avoids high-hazard risks and high-hazard lines of business such as medical malpractice and environmental liability.

Penn-America markets its products through fifty-seven (57) general agents, who in turn produce business through more than 25,000 retail insurance brokers located throughout the United States. The Company focuses on serving the insurance needs of small businesses in small towns and rural areas that are serviced by retail insurance brokers with limited access to larger, standard lines insurers. The Company believes that larger, standard lines insurers, which often limit their underwriting to larger policies and to certain risk classes, generally underserve these markets. Penn-America believes that its distribution network enables it to effectively access these numerous small markets at a relatively low fixed-cost through the marketing, underwriting and administrative support of its general agents. This access also is enabled by the local market knowledge and expertise of these general agents and their retail insurance brokers.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Penn-America's distribution strategy is to maintain strong relationships with a select group of high-quality general agents. The Company carefully selects a limited number of general agents based on their experience and reputation and strives to preserve each agent's franchise value within its marketing territory. The Company seeks to grow with these general agents and develop strong, long-standing relationships by providing a high level of service and support. The success of the Company's strategy is demonstrated by its strong and consistent growth. From 1992 to 2001, commercial gross written premiums grew at an 18% compound annual rate from \$22.6 million to \$98.4 million while the number of general agents rose from 38 to 57.

Core Commercial Business

The Company underwrites its core commercial business (excluding the Company's exited commercial automobile business - see Exited Lines, below) on a Binding Authority, Submit and Specialty Lines basis, which are defined as follows:

- o Binding authority business represents risks that may be quoted and bound by the Company's general agents prior to the Company's underwriting review.

Page 4

- o Submit business represents risks that must be submitted by the Company's general agents to the Company prior to quoting or binding the account.
- o Specialty lines business represents risks that meet specific, pre-determined industry-segment and territorial parameters and may be quoted or bound by the Company's general agents prior to the Company's underwriting review.

Binding Authority business accounted for approximately 88% of the Company's core commercial gross written premiums in 2001. Of this amount, approximately 85% is bound by general agents in accordance with the Company's underwriting manual. New and renewal Binding Authority business issued by the general agents is reviewed on a continuous basis to ensure that the Company's underwriting guidelines are followed. The Company provides its general agents with a comprehensive, regularly updated underwriting manual, which also is available online through a private intranet site called PennLink. This manual clearly outlines the Company's risk eligibility, pricing, underwriting guidelines and policy issuance instructions. Penn-America closely monitors the underwriting quality of its business through online system edits and in-force account reviews. The Company also periodically audits each agent's office to determine if the Company's underwriting guidelines are followed in all aspects of risk selection, underwriting compliance, policy issuance and pricing. In addition to standard commissions, the Company provides strong incentives to its general agents to produce profitable business through a contingent profit commission structure that is tied directly to underwriting profitability. Payments of these contingent profit commissions have been through the issuance of shares of PAGI common stock and cash. Since 1996, the Company has awarded agents approximately 276,000 shares of PAGI common stock through its contingent profit commission structure.

The Company began writing business on a Submit basis in 1999 in response to general agents who had risks similar to the Company's risk profile but were outside of their underwriting authority. This provides a market to the Company's general agents for approximately fifty classes of business. One hundred percent

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

of the business is quoted and bound by Penn-America underwriters; general agents have no binding authority. This business accounted for approximately 5% of core commercial gross written premiums in 2001.

Specialty Lines business, which accounted for 7% of the Company's core commercial gross written premiums in 2001, represents specialized underwriting and marketing programs for individual general agents based upon specific territorial needs and opportunities. An individual general agent typically is given exclusive marketing authority for a special program subject to territorial limitations. The Company believes it can achieve superior underwriting results and expense savings on these programs. The Company continuously is developing specialized programs for certain industry segments to meet the needs of insureds in these segments. For example, Penn-America has developed programs for cargo and Alaskan dwellings. Collectively, these programs are a significant benefit to Penn-America's marketing efforts.

Exited Lines

The Company offered commercial automobile coverage from 1998 through the first quarter of 2001. In late 2000, the Company announced that it was exiting this line of business due to unsatisfactory underwriting results. No new policies have been written since the first quarter of 2001 and all policies are being non-renewed. Gross written premiums for commercial automobile business decreased to \$1.1 million in 2001 from \$11.5 million in 2000 and \$7.0 million in 1999.

The Company exited the non-standard personal automobile business in 1999 and, as a result, gross written premiums declined to \$2,000 in 2001 from \$2.8 million in 2000 and \$11.5 million in 1999.

Page 5

Financial Information About Business Segments

The Company has two reportable segments: personal lines and commercial lines. The Company exited the non-standard personal automobile business in 1999 and announced that it would run-off its remaining portfolio of such business. The Company will continue to report on this segment separately until the amounts relating to the non-standard personal automobile business become immaterial to the financial statements presented. These segments were managed separately because they have different customers, pricing and expense structures. The Company does not allocate assets between segments because assets are reviewed in total by management for decision-making purposes.

The accounting policies of the segments are the same as those more fully described in the summary of significant accounting policies in Note 1 to the consolidated financial statements, included herein. The Company evaluates segment profit based on profit or loss from operating activities. Segment profit or loss from operations is pre-tax and does not include unallocated expenses but does include investment income attributable to insurance transactions. Segment profit or loss therefore excludes income taxes, unallocated expenses and investment income attributable to equity. The aforementioned segment information is presented in Note 8 to the consolidated financial statements included herein.

The following table sets forth the geographic distribution of the Company's gross written premiums for the periods indicated:

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

(Dollars in Thousands)	Years ended December 31,			
	2001		2000	
	Amount	Percent	Amount	Percent
Pacific	\$ 15,613	15.9%	\$ 19,961	18.2%
Midwest	17,338	17.6	21,768	19.8
South	17,021	17.3	16,539	15.1
Southwest	12,306	12.5	15,532	14.1
Mid-Atlantic	17,633	17.9	17,253	15.7
Mountain/Northwest	8,088	8.2	10,457	9.5
New England	10,413	10.6	8,281	7.6
	<u>\$ 98,412</u>	<u>100.0%</u>	<u>\$109,791</u>	<u>100.0%</u>

Page 6

Lines of Business

The following table sets forth an analysis of gross written premiums by specific product lines during the periods indicated:

(Dollars in thousands)	Years ended December 31,			
	2001		2000	
	Amount	Percent	Amount	Percent
Core commercial lines				
Special property	\$10,118	10.3%	\$5,930	5.4
CMP - property	36,381	37.0	32,677	29.8
CMP - liability	27,348	27.8	27,660	25.2
Other & product liability	23,483	23.8	29,268	26.6
Total core commercial	<u>97,330</u>	<u>98.9</u>	<u>95,535</u>	<u>87.0</u>
Exited lines				

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Commercial auto liability	874	0.9	8,779	8.0
Commercial auto physical damage	206	0.2	2,690	2.5
Personal lines	2	-	2,787	2.5
	-----	-----	-----	-----
Total exited lines	1,082	1.1	14,256	13.0
	-----	-----	-----	-----
Total gross written premiums	\$ 98,412	100.0%	\$109,791	100.0
	=====	=====	=====	=====

- o The Company's Commercial General Liability insurance is written on an occurrence policy form, which generally provides coverage for bodily injury or property damage that arises during the policy period, even though a claim is made after the policy expires, as opposed to a claims-made policy form, which generally provides coverage for claims made against an insured during the policy period, irrespective of when the bodily injury or property damage occurred. The Company's insurance coverage provides limits generally ranging from \$25,000 to \$3 million per occurrence, with the majority of such policies having limits between \$500,000 and \$1 million. The Company's general liability policies provide for defense and related expenses in addition to per occurrence and aggregate policy limits.
- o The Company's Commercial Property lines provide limits usually no higher than \$2 million per risk, with almost all of the policies being written at limits of \$1 million per risk or less.
- o The Company writes Commercial Multi-Peril policies that provide the same commercial property and general liability coverages bundled together as a "package" for its insureds. The limits on these policies are the same as if written on a monoline basis.
- o The Company also offers Commercial Umbrella policies to enhance its commercial multi-peril and commercial general liability writings. Commercial umbrella insurance is written for limits up to \$5 million per occurrence. For commercial umbrella coverage, Penn-America usually writes the primary \$1 million liability limit.
- o Commercial Automobile policies were written with liability limits up to \$1 million per occurrence.
- o Non-Standard Personal Automobile policies were written with liability limits up to \$100,000 per person and \$300,000 per occurrence.

Pricing

In the commercial property and casualty market, the rates and terms of coverage provided by property and casualty insurance carriers are frequently based on benchmarks and forms promulgated by the Insurance Services Office ("ISO"). ISO makes available to its members advisory rating, statistical and actuarial services, policy language and other related services. ISO currently provides such services to more than 1,500 property and casualty insurance companies in

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

the U.S. One of the services that ISO provides is an actuarial-based estimate of the expected loss cost for risks in each of approximately 1,000 risk classifications. These benchmark loss costs reflect an analysis of the loss and allocated loss adjustment expenses on claims reported to ISO. ISO statistics, however, include only claims and policy information reported to ISO, and therefore do not reflect all of the loss experience for each class. Also, the historical results for a particular class may not be sufficient to provide actuarially meaningful results.

The Company primarily uses ISO statistics as a benchmark for risk selection and pricing. Other carriers may or may not rely as heavily on this information, and several of the larger standard carriers have developed their own actuarial databases. As a general rule, most standard lines insurers set rates lower than ISO benchmarks. However, the Company, because of its strategy of providing insurance to underserved markets, typically charges 100% or more of prescribed ISO benchmarks. Generally, the Company establishes a pricing strategy on a countrywide basis that is designed to support its loss costs and operating expenses plus a targeted return on equity. This pricing strategy is regionalized to incorporate variables such as historical loss experience, the types and lines of business written and state regulatory considerations. The Company provides its general agents with pricing flexibility on a per-policy basis, with the objective that in the aggregate, the weighted average premium of all new and renewal commercial policies written by a general agent are at approximately 110-150% of ISO benchmarks.

Claims Management and Administration

Commercial Claims:

The Company's approach to commercial claims management is designed to investigate reported incidents at the earliest juncture, to select, manage and supervise all legal and adjustment aspects thereof and to provide a high level of service and support to general agents, retail insurance brokers and insureds throughout the claims process. The Company's commercial general agents have no authority to settle commercial claims or otherwise exercise control over the claims process. All commercial lines claims are supervised and processed centrally by the Company's claims management staff. Senior claims management reviews all claims greater than \$25,000.

Discontinued Personal Automobile Claims:

All claims for the personal automobile business are handled by the Company's internal claims unit. Prior to February 1, 2000, if an automobile claim was in the States of California or Washington, they were handled by outside third-party claims management companies.

Insurance Loss Reserves

The Company is directly liable for losses and loss adjustment expenses under the terms of the insurance policies that it writes. In many cases, several years may lapse between the occurrence of an insured loss, the reporting of the loss to the Company and the Company's payment of that loss. The Company reflects its liability for the ultimate payment of all incurred losses and loss adjustment expenses by establishing loss and loss adjustment expense reserves as balance sheet liabilities for both reported and unreported claims.

When a claim involving a probable loss is reported, the Company establishes a

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

case reserve for the estimated amount of the Company's ultimate loss. The estimate of the amount of the ultimate loss is based upon such factors as the type of loss, jurisdiction of the occurrence, knowledge of the circumstances surrounding the claim, severity of injury or damage, potential for ultimate exposure and policy provisions relating to the claim. Loss adjustment expenses are determined via a formula method that estimates loss adjustment expenses as a percentage of expected indemnity losses based on historical patterns adjusted to current experience.

In addition to case reserves, management establishes reserves on an aggregate basis to provide for incurred but not reported losses and loss adjustment expenses ("IBNR"). The establishment of reserves for IBNR requires an estimate of the ultimate liability based primarily on past experience. The Company applies a variety of traditional actuarial techniques to determine its estimate of ultimate liability. The techniques recognize, among other factors, the Company's and the industry's experience, historical trends in reserving patterns and loss payments, the impact of claim inflation, the pending level of unpaid claims, the cost of claim settlements, the line of business mix and the economic environment in which property and casualty insurance companies operate. Estimates continually are reviewed and, based on new developments and new information, adjustments of the probable ultimate liability are included in operating results for the periods in which the adjustments are made. In general, reserves are established initially based upon the actuarial and underwriting data utilized to set pricing levels and are reviewed as additional information, including claims experience, becomes available. The establishment of loss and loss adjustment expense reserves makes no provision for the broadening of coverage by legislative action or judicial interpretation or for the extraordinary future emergence of new types of losses not sufficiently represented in the Company's historical experience, or which cannot yet be quantified. The Company regularly analyzes its reserves and reviews its pricing and reserving methodologies so that future adjustments to prior year reserves can be minimized. However, given the complexity of this process, reserves will require continual updates and the ultimate liability may be higher or lower than previously indicated. The Company does not discount its loss reserves.

Activity in the liability for unpaid losses and loss adjustment expenses is summarized as follows:

	Year ended December 31,		
	2001	2000	1999
	(in thousands)		
Balance, beginning of year	\$115,314	\$93,719	\$88,937
Less reinsurance recoverable	24,093	18,086	16,502
Net balance, beginning of year	91,221	75,633	72,435
Incurred related to:			
Current year	60,885	66,214	54,768
Prior years	36	9,164	8,419
Total incurred	60,921	75,378	63,187
Paid related to:			
Current year	19,913	26,273	23,540
Prior years	38,183	33,517	36,449
Total paid	58,096	59,790	59,989
Net balance, end of year	94,046	91,221	75,633
Plus reinsurance recoverable	25,552	24,093	18,086

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

	-----	-----	-----
Balance, end of year	\$119,598	\$115,314	\$93,719
	=====	=====	=====

In 2001, the Company increased incurred losses and loss adjustment expenses attributable to insured events of prior years by \$36,000. This increase related entirely to the commercial automobile line of business. During 2001, the Company increased its estimate for the commercial multi-peril liability line of business by \$1.8 million due to the development of outstanding claim reserves on claims occurring primarily in 1998 and 1999.

Page 9

This increase was almost entirely offset by a reduction in the Company's estimate for the non-standard personal automobile line of business due to favorable settlements on closed claims.

In 2000, the Company increased incurred losses and loss adjustment expenses attributable to insured events of prior years by \$9,164,000. The increase is primarily attributable to changes in the Company's estimates for losses and loss adjustment expense reserves of \$1,400,000 for commercial automobile, \$3,900,000 for commercial multi-peril liability and \$3,400,000 for other liability lines of business.

The Company began writing commercial automobile coverage for vehicles and light trucks in 1998. The initial estimates for 1998 and 1999 were based on a relatively low level of claims reported to the Company. In 2000, the Company received a significant number of claims relating to accidents incurred in 1998 and 1999. In the fourth quarter of 2000, the Company exited the commercial automobile line of business due to unsatisfactory underwriting results.

The change in estimates in 2000 for the commercial multi-peril liability line of business resulted principally from increased exposure to liquor liability losses for policies primarily written in 1998 and 1999. In 2000, the Company revised its underwriting approach significantly to reduce its exposure to liquor liability.

The change in estimates in 2000 for the other liability line resulted principally from construction defect claims, which were new types of claims that were not anticipated when the Company wrote these policies between 1991 and 1996. These claims predominantly related to residential contractors and sub-contractors in California. In 2000, the Company completed its withdrawal from the residential contractors and sub-contractors industry segment.

In 1999, the Company increased incurred losses and loss adjustment expenses attributable to insured events of prior years by \$8,419,000. The increase is primarily attributable to changes in estimates for losses and loss adjustment expense reserves for non-standard personal automobile line of business. In 1999, the Company received a significant number of claims relating to accidents incurred prior to 1999, resulting in an increase in loss estimates. In 1999, the Company exited the non-standard personal automobile lines.

Incurred losses and loss adjustment expenses include estimates, recorded as loss and loss adjustment expense reserves on the balance sheet, for the ultimate payment on both reported and unreported claims. The Company changes its estimates for loss and loss adjustment expenses reserves as new events occur, as more loss experience is acquired or as additional information is received.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Estimates for loss and loss adjustment expense reserves result from a continuous review process and the change in these estimates, as required by Financial Accounting Standards Board No. 60, Accounting and Reporting by Insurance Enterprises, paragraph 18, is recorded in the period that the change in these estimates is made.

The Company believes that its loss and loss adjustment expense reserves are fairly stated as of December 31, 2001 due to the exiting of non-standard personal and commercial automobile lines of business and the reduction in exposure to construction defect and liquor liability losses. In addition, the Company implemented improvements in the loss reserving process, including the development of monthly and quarterly loss and loss adjustment expense reserve analyses and the creation of a reserve committee that meets quarterly.

The following table presents the Company's accident year loss and loss adjustment expense ratios (the sum of losses and loss adjustment expenses divided by premiums earned) for the ten most recent accident years (the year in which the loss occurred), as recorded as of December 31, 1999, 2000 and 2001 after giving effect to the increase in loss and loss adjustment expenses relating to changes in estimates of insured events of prior years. These "accident year" loss ratios differ from the loss ratios included in the Company's financial statements set forth elsewhere in this report in that the

Page 10

latter loss ratios are based upon the year in which losses are recognized for accounting purposes, regardless of when the loss actually occurred or was reported. See the notes to the consolidated financial statements included herein.

Accident Year	As of December 31,		
	1999	2000	2001
1992	69.6	72.1	72.5
1993	70.9	70.2	71.3
1994	69.1	72.0	71.8
1995	63.9	65.4	65.1
1996	68.1	68.3	69.4
1997	62.4	62.0	62.1
1998	63.6	65.8	65.0
1999	63.8	68.2	70.0
2000		72.4	70.2
2001			68.5

The following table represents the development of unpaid loss and loss adjustment expense reserves during the ten years ended December 31, 2001. The top of the table reflects the ten-year development of the Company's reserves, net of reinsurance. The bottom of the table reconciles 1992 through 2001 ending reserves to the gross reserves in the Company's consolidated financial statements. Prior to 1992, the Company developed its reserves on a net of reinsurance basis and restatement for those prior years is not presented. The top line of the table shows the estimated reserve for unpaid loss and loss adjustment expenses at the balance sheet date for each of the indicated years. These figures represent the estimated amount of unpaid loss and loss adjustment expenses for claims arising in all prior years that were unpaid at the balance

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

sheet date, including losses that had been incurred but not yet reported. The table also shows the re-estimated amount of the previously recorded reserve based on experience as of the end of each succeeding year. The estimate changes as more information becomes available about the frequency and severity of claims. The cumulative redundancy or deficiency represents the aggregate change in the reserve estimates over all prior years.

Page 11

	1991	1992	1993	1994	1995	1996	1997	1998
Reserves for unpaid losses and loss adjustment Expenses, as stated (In thousands)	\$25,681	\$26,110	\$26,830	\$35,307	\$46,512	\$55,656	\$68,863	\$72,000
a. Net cumulative paid as of								
1 year later	\$6,605	\$7,381	\$6,852	\$12,383	\$17,208	\$23,660	\$30,236	\$36,000
2 years later	10,988	11,127	13,127	20,617	29,612	38,819	51,141	55,000
3 years later	13,325	15,546	18,656	27,266	38,091	50,982	63,470	70,000
4 years later	16,417	19,253	22,254	32,119	44,016	57,613	72,651	
5 years later	19,283	21,503	24,303	34,883	48,236	62,724		
6 years later	20,872	22,796	25,642	37,687	51,485			
7 years later	21,881	23,714	27,121	39,863				
8 years later	22,452	24,959	28,449					
9 years later	23,303	25,979						
10 years later	24,006							
b. Reserves re-estimated as of end of year								
1 year later	\$23,228	\$24,478	\$23,897	\$33,601	\$45,708	\$55,997	\$68,946	\$80,000
2 years later	22,383	21,945	23,489	34,281	47,225	57,913	76,217	86,000
3 years later	20,471	22,032	24,558	36,453	47,378	63,575	79,881	86,000
4 years later	20,819	22,767	26,335	36,359	50,704	67,310	81,226	
5 years later	21,726	23,935	26,380	38,768	54,245	68,567		
6 years later	22,550	24,143	27,532	41,425	54,740			
7 years later	22,761	24,776	29,050	42,095				
8 years later	23,117	26,485	29,804					
9 years later	24,280	26,948						
10 years later	24,644							
Net cumulative redundancy (deficiency)	\$1,037	(\$839)	(\$2,974)	(\$6,788)	(\$8,228)	(\$12,911)	(\$12,363)	(\$14,000)
Gross liability for unpaid losses and loss adjustment expenses, as stated		\$31,703	\$33,314	\$44,796	\$60,139	\$70,728	\$84,566	\$88,000

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Reinsurance recoverable	5,593	6,484	9,489	13,627	15,072	15,703	16,250
Net liability for unpaid losses and loss adjustment expenses, as stated	26,110	26,830	35,307	46,512	55,656	68,863	72,250
<hr/>							
Gross liability re-estimated - 1 year later	30,609	32,796	48,173	63,884	71,644	85,640	98,250
Reinsurance recoverable re-estimated	6,131	8,899	14,572	18,176	15,647	16,694	17,250
Net liability re-estimated - 1 year later	24,478	23,897	33,601	45,708	55,997	68,946	80,250
<hr/>							
Gross liability re-estimated - 2 years later	30,390	36,243	53,009	66,405	74,312	92,832	104,250
Reinsurance recoverable re-estimated	8,445	12,754	18,728	19,180	16,399	16,615	18,250
Net liability re-estimated - 2 years later	21,945	23,669	34,281	47,225	57,913	76,217	86,250
<hr/>							
Gross liability re-estimated - 3 years later	33,992	41,600	56,042	66,891	80,574	97,786	105,250
Reinsurance recoverable re-estimated	11,960	17,042	19,589	19,513	16,999	17,905	18,250
Net liability re-estimated - 3 years later	22,032	24,558	36,453	47,378	63,575	79,881	86,250
<hr/>							
Gross liability re-estimated - 4 years later	38,165	43,824	56,167	68,927	84,831	98,244	105,250
Reinsurance recoverable re-estimated	15,398	17,489	19,808	18,223	17,521	17,018	18,250
Net liability re-estimated - 4 years later	22,767	26,335	36,359	50,704	67,310	81,226	86,250
<hr/>							
Gross liability re-estimated - 5 years later	39,956	44,466	58,272	73,042	85,221	92,250	105,250
Reinsurance recoverable re-estimated	16,021	18,086	19,504	18,797	16,654	16,654	18,250
Net liability re-estimated - 5 years later	23,935	26,380	38,768	54,245	68,567	75,596	86,250
<hr/>							
Gross liability re-estimated - 6 years later	40,670	45,595	61,814	72,978	80,250	85,250	105,250
Reinsurance recoverable							18,250

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

re-estimated	16,527	18,063	20,389	18,238				
Net liability re-estimated - 6 years later	24,143	27,532	41,425	54,740				
Gross liability re-estimated - 7 years later	41,679	47,955	61,766					
Reinsurance recoverable re-estimated	16,903	18,905	19,671					
Net liability re-estimated - 7 years later	24,776	29,050	42,095					
Gross liability re-estimated - 8 years later	43,958	48,032						
Reinsurance recoverable re-estimated	17,473	18,228						
Net liability re-estimated - 8 years later	26,485	29,804						
Gross liability re-estimated - 9 years later	44,248							
Reinsurance recoverable re-estimated	17,300							
Net liability re-estimated - 9 years later	26,948							
Gross cumulative deficiency	(\$12,545)	(\$14,718)	(\$16,970)	(\$12,838)	(\$14,493)	(\$13,678)	(\$16,970)	

Page 12

The table below illustrates the sensitivity to a hypothetical change in the Company's net loss and loss adjustment expense reserves as of December 31, 2001. The selected scenarios are not predictions of future events, but rather illustrative of the effect that such events may have on stockholders' equity.

Hypothetical Change in Net Loss and Loss Adjustment Expense Reserve	Balance of Net Loss and Loss Adjustment Expense Reserves	Change in Net Loss and Loss Adjustment Expense
3% increase	\$96,867	\$2
2% increase	95,927	1

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

1% increase	94,986	
No change	94,046	
1% decrease	93,106	
2% decrease	92,165	(1)
3% decrease	91,225	(2)

The following table sets forth ratios for the Company and the industry prepared in accordance with statutory accounting practices ("SAP") prescribed or permitted by state insurance authorities. The statutory combined ratio, which reflects underwriting results but not investment income, is a traditional measure of the underwriting performance of a property and casualty insurer. This ratio is the sum of (i) the ratio of incurred losses and loss adjustment expenses to net earned premium ("loss ratio"); and (ii) the ratio of expenses incurred for commissions, premium taxes, administrative and other underwriting expenses to net written premium ("expense ratio").

	Years ended December 31	
	2001	2000
The Company:		
SAP Basis (3)		
Loss and loss adjustment expense ratio	68.5	82.4
Expense ratio	33.6	33.2
Combined ratio	102.1	115.6

	Years ended December 31		
	2001 (1)	2000 (2)	1999 (3)
Property and casualty insurance industry :			
SAP Basis (3)			
Loss and loss adjustment expense ratio	88.0	81.5	
Expense ratio	25.9	27.5	
Dividend ratio	.5	1.4	
Combined ratio	114.4	110.4	

(1) Source: Industry Estimate for 2001, BestWeek, December 17, 2001 edition.

(2) Source: Best's Aggregates & Averages, Property/Casualty United States 2001 Edition

(3) While the SAP loss ratio is the same ratio as the loss ratio prepared in accordance with generally accepted accounting principles ("GAAP"), the expense ratio differs in two aspects. First, the numerator on a SAP basis represents acquisition and other underwriting expenses relating to net written premiums recorded during the calendar year, while, on a GAAP basis, the numerator represents amortization of deferred policy acquisition costs and other underwriting expenses. Second, the denominator on a SAP basis is net written premiums, versus net earned premium on a GAAP basis.

Reinsurance

The Company purchases reinsurance through contracts called "treaties" to reduce its exposure to liability on individual risks and to protect against catastrophic losses. Reinsurance involves an insurance company transferring or "ceding" a portion of its exposure on a risk to another insurer (the "reinsurer"). The reinsurer assumes the exposure in return for a portion of the premium. The ceding of liability to a reinsurer does not legally discharge the primary insurer from its liability for the full amount of the policies on which it obtains reinsurance. The primary insurer will be required to pay the entire loss if the reinsurer fails to meet its obligations under the reinsurance agreement.

In formulating its reinsurance programs, the Company is selective in its choice of reinsurers and considers numerous factors, the most important of which are the financial stability of the reinsurer, its history of responding to claims and its overall reputation. In an effort to minimize its exposure to the insolvency of its reinsurers, the Company evaluates the acceptability and reviews the financial condition of each reinsurer annually. The Company's policy is to use only reinsurers that have an A.M. Best rating of "A- (Excellent)" or better and that have at least \$500 million in policyholders' surplus. A.M. Best assigns ratings to each insurance company transacting business in the United States. "A-" is the fourth highest of sixteen rating categories, and is considered "excellent" by A.M. Best Co. These ratings are based upon factors of concern to policyholders and are not directed toward the protection of investors.

Since September 2001, the Company's multiple-line excess of loss treaty reinsurance is with American Re, part of the Munich Re Group. American Re is rated "A++" (Superior) by A.M. Best. For the three years prior to September 1, 2001, General Reinsurance Corporation, rated "A++" (Superior) by A.M. Best, was the Company's reinsurer on their multiple-line excess of loss treaty. The following is a summary of the Company's multiple-line excess of loss reinsurance treaty:

Line of Business	Company Policy Limit	Reinsurance Coverage / Comp
Property	\$2.0 million per risk	\$1.7 million per risk in exc
Commercial Automobile	\$1.0 million per occurrence	\$750,000 per occurrence in e occurrence
General Liability	\$3.0 million per occurrence	\$2.5 million per occurrence occurrence

The combined Company retention for any one loss resulting from a common occurrence involving both the property and general liability coverage on a single risk is \$500,000. The Company also maintains casualty contingent excess coverage with American Re, which covers exposures such as punitive damages and other extra-contractual obligations, losses in excess of policy limits (such as bad faith and errors and omissions) and liability actions brought by two or more of the Company's insureds against each other resulting from the same occurrence.

The Company offers umbrella liability policies up to \$5.0 million per occurrence. These policies are reinsured with American Re for 90% of policy

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

limits up to \$1.0 million per occurrence and 100% of policy limits to \$4.0 million in excess of \$1.0 million per occurrence.

The Company maintains a catastrophic loss reinsurance program, the terms of which provide for 100% retention of the first \$1.0 million per occurrence,

Page 14

reinsurance of 90.0% of \$1.0 million per occurrence in excess of \$1.0 million per occurrence and reinsurance of 100% of \$23.0 million per occurrence in excess of \$2.0 million per occurrence.

As of January 1, 2002, the Company's catastrophic loss reinsurance program includes: American Agricultural Insurance Company, Converium (North America), Converium (UK), Everest Reinsurance Company, Hannover Ruckversicherungs, PXRE Reinsurance Company, Shelter Reinsurance Company, Sirius International Insurance Corporation and XL Re Ltd. All of these reinsurers are rated A- (Excellent) or higher by A.M. Best and have policyholders' surplus greater than \$500 million.

The Company may write individual policies with limits of liability greater than the aforementioned Company policy limits. These limits of liability are 100% reinsured on a facultative reinsurance basis.

Information regarding the amount of premiums written and ceded under reinsurance treaties is included in Note 5 to the Consolidated Financial Statements included herein.

Investments

The Company's investment policy seeks to maximize investment income consistent with the overriding objective of maintaining liquidity and minimizing risk. Approximately 93% of the Company's fixed-income securities as of December 31, 2001 were rated "A" or better by Standard & Poor's. Standard & Poor's rates publicly traded securities in twenty categories ranging from AAA to CC. Securities with ratings from AAA to BBB- (the top ten categories) are commonly referred to as having an investment grade rating. As of December 31, 2001, the Company's fixed-income investments had an effective average duration of approximately 3.5 years. Publicly traded equity securities, the majority of which consisted of preferred stocks, represented 16% of the Company's investment portfolio as of December 31, 2001.

As of December 31, 2001, the Company's investment portfolio contained \$48.8 million of mortgage-backed and asset-backed and collateral mortgage obligations. All of these securities were rated "AA-" or better by Standard & Poor's or Moody's and 75% were "AAA" or better by Standard & Poor's or Moody's, are publicly traded, and have market values obtained from an external pricing service. Changes in estimated cash flows due to changes in prepayment assumptions from the original purchase assumptions are revised based on current interest rates and the economic environment. Although the Company is permitted to invest in other derivative financial instruments, real estate mortgages and real estate, the Company does not invest in these financial instruments and does not have any such investments in its investment portfolio.

The Company's investment portfolio is under the direction of its Investment Committee, which is comprised of selected members of the Company's Board of Directors and officers of the Company. The Investment Committee establishes and monitors the Company's investment policies, which are intended to maximize after-tax income while maintaining a high level of quality and liquidity in its

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

portfolio for insurance operations. All investment transactions are approved by the Investment Committee.

The Investment Committee has retained General Re-New England Asset Management, Inc, a wholly owned subsidiary of General Re Corporation, to manage its investment portfolio in accordance with the investment strategy adopted by the Investment Committee.

Page 15

The following table shows the classifications of the Company's investments at December 31, 2001:

	Fair value	Amount reflected on balance sheet (In thousands)	Percent total
Fixed maturities:			
Available for sale:			
U.S. Treasury securities and obligations of U.S. government agencies	\$ 4,195	\$ 4,195	2
Corporate securities	52,021	52,021	29
Mortgage-backed securities	27,316	27,316	15
Other structured securities	21,462	21,462	12
Municipal securities	21,004	21,004	12
Public utilities	9,255	9,255	5
Total available for sale	135,253	135,253	77
Held to maturity			
U.S. Treasury securities and obligations			
of U.S. government agencies	14,025	13,812	7
Corporate securities	290	276	0
Public utilities	1,002	996	0
Total held to maturity	15,317	15,084	8
Total fixed-maturity securities	150,570	150,337	85

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Equity securities:			
Common stock	7,977	7,977	4
Preferred stock	17,172	17,172	9
	-----	-----	-----
Total equity securities	25,149	25,149	14
	-----	-----	-----
Total investments	\$175,719	\$175,486	100
	=====	=====	=====

The composition of the Company's portfolio of fixed-income investments were rated by Standard & Poor's or Moody's at December 31, 2001, as follows:

"AAA"	50%
"AA"	18%
"A"	25%
"BBB"	6%
Below "BBB"	1%

	100%
	=====

The market risk of the Company's investment portfolio is described in Quantitative and Qualitative Disclosures About Market Risk included herein.

Note 4 to the consolidated financial statements included herein sets forth the net investment income results of the Company for 2001, 2000 and 1999.

Competition

The property and casualty insurance industry is highly competitive and includes several thousand insurers, ranging from large companies offering a wide variety of products worldwide to smaller, specialized companies in a single state or region and offering in some cases only a single product. The Company competes with a significant number of these insurers in attracting quality general agents and in selling insurance products. Many of the Company's existing or potential competitors are larger excess and surplus lines and specialty admitted insurers which have considerably greater financial and other resources, have greater experience in the insurance industry and offer a broader line of insurance products than the Company. The Company believes that in order to be successful in its market, it must be aware of pricing cycles, must be able to minimize the impact of such cycles through tight expense control and superior customer service. Another competitive factor is the rating assigned by independent rating organizations such as A.M. Best Company. Penn-America and Penn-Star currently have a pooled rating from A.M. Best of "A-" (Excellent). "A-" is the fourth highest of sixteen rating categories, and is considered "excellent" by A.M. Best Co. These ratings are based upon factors of concern to policyholders and are not directed toward the protection of investors.

The Company believes that its distribution strategy, which is based on building and maintaining strong relationships with a small number of high quality general

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

agents that are enabled with the latest technological innovation, provides a competitive advantage in the markets it targets. The "Marketing and Distribution" section included herein more fully describes the elements of the strategies which the Company believes provide this competitive advantage.

Regulation

General. The Company is subject to regulation under the insurance statutes and regulations, including insurance holding company statutes, of the various states in which it does business. These statutes are generally designed to protect the interests of insurance policyholders, as opposed to the interests of stockholders, and they relate to such matters as the standards of solvency which must be met and maintained; the licensing of insurers and their agents; the nature and limitations of investments; deposits of securities for the benefit of policyholders; approval of policy forms and premium rates; periodic examination of the affairs of insurance companies; annual and other reports required to be filed on the financial condition of insurers or for other purposes; establishment and maintenance of reserves for unearned premiums and losses; and requirements regarding numerous other matters. All insurance companies must file annual statements with certain state regulatory agencies and are subject to regular and special financial examinations by those agencies. The last regulatory financial examination of Penn-America was completed by the Pennsylvania Insurance Department in 1999, covering the five-year period ended December 31, 1998, and for Penn-Star, covering a two year period ended December 31, 1998, since its initial licensing in 1997.

Insurance Holding Company Laws. Pennsylvania, the Companies' state of domicile, has laws governing insurers and insurance holding companies. The Pennsylvania statutes generally require insurers and insurance holding companies to register and file reports concerning their capital structure, ownership, financial condition and general business operations. Under the statutes, a person must generally obtain the Pennsylvania Insurance Department's approval to acquire, directly or indirectly, 10% or more of the outstanding voting securities of the company or any of its insurance company subsidiaries. The insurance department's determination of whether to approve any such acquisition is based on a variety of factors, including an evaluation of the acquirer's financial condition, the competence of its management and whether competition would be reduced. All transactions within a holding company's group affecting an insurer must be fair and reasonable and the insurer's policyholders' surplus following any such transaction must be both reasonable in relation to its outstanding liabilities

Page 17

and adequate for its needs. Notice to applicable regulators is required prior to the consummation of certain transactions affecting insurance subsidiaries of the holding company group.

Dividend Restrictions. PAGI is a holding company, the principal asset of which is the common stock of Penn-America. The principal source of cash to meet the Company's short-term liquidity needs, including the payment of dividends to PAGI's stockholders and PAGI's operating expenses is dividends from Penn-America. The Company has no long-term debt obligations or planned capital expenditures that could impact its long-term liquidity needs. Penn-America's principal sources of funds are underwriting operations, investment income and proceeds from sales and redemptions of investments. Funds are used by Penn-America and Penn-Star principally to pay claims and operating expenses, to purchase investments and to make dividend payments to PAGI. The Company's future liquidity is dependent on the ability of Penn-America to pay dividends to PAGI.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

The National Association of Insurance Commissioners has adopted a system to test the adequacy of statutory capital, known as "risk-based capital", which applies to Penn-America Insurance Company and Penn-Star Insurance Company, Penn-America Insurance Company's wholly-owned subsidiary. This system establishes the minimum amount of risk-based capital necessary for a company to support its overall business operations. It identifies property and casualty insurers that may be inadequately capitalized by looking at certain inherent risks of each insurer's assets and liabilities and its mix of net written premiums. Insurers falling below a calculated threshold may be subject to varying degrees of regulatory action, including supervision or control. Penn-America is also subject to regulations under which payment of dividends from statutory surplus may require prior approval from the Pennsylvania Insurance Department. Penn-America may pay dividends to PAGI without advance regulatory approval only from unassigned surplus and only to the extent that all dividends in the past twelve months do not exceed the greater of 10% of total statutory surplus or statutory net income for the prior year. Using these criteria, the available ordinary dividend for 2002 is \$6,473,325. Ordinary dividends paid by Penn-America to PAGI in 2001 were \$1.6 million. No ordinary dividends were paid to PAGI in 2000. Rather, Penn-America paid a \$6.4 million return of capital to PAGI in 2000, after receiving approval from the Pennsylvania Insurance Department, which PAGI used to repurchase stock and pay dividends and PAGI operating expenses. Penn-America's ability to pay future dividends to us without advance regulatory approval is dependent upon maintaining a positive level of unassigned and policyholders' surplus, which in turn, is dependent upon Penn-America Insurance Company and Penn-Star Insurance Company generating net income in excess of dividends to the Company. As of December 31, 2001, Penn-America Insurance Company's unassigned surplus was \$64,733,251 million and Penn-Star Insurance Company's policyholders' surplus was \$33,389,965 million.

Insurance Guaranty Funds. Under insolvency or guarantee laws in states in which Penn-America is licensed as an admitted insurer (and in New Jersey), organizations have been established (often referred to as guaranty funds) with the authority to assess admitted insurers up to prescribed limits for the claims of policyholders insured by insolvent, admitted insurance companies. Surplus lines insurance companies are generally not subject to such assessments except in New Jersey and their policyholders are not eligible to file claims against the guaranty funds.

Additional Legislation or Regulations. New regulations and legislation are proposed from time to time to limit damage awards, to bring the industry under regulation by the federal government, to control premiums, policy terminations and other policy terms, and to impose new taxes and assessments. Difficulties with insurance availability and affordability have increased legislative activity at both the federal and state levels. Some state legislatures and regulatory agencies have enacted measures, particularly in personal lines, to

Page 18

limit midterm cancellations by insurers and require advance notice of renewal intentions. In addition, Congress is investigating possible avenues for federal regulation of the insurance industry.

Employees

The Company has approximately 100 employees. The Company is not a party to any collective bargaining agreements and believes that its employee relations are good.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Item 2. Properties

The Company leases approximately 23,000 square feet in an office building located in Hatboro, Pennsylvania. The office building also houses Penn Independent and certain of its subsidiaries. The Company leases the space from Mr. Irvin Saltzman, Chairman of the Board of Directors of the Company, pursuant to a lease agreement renewed June 30, 2000 that expires on June 30, 2005, and provides for an annual rental payment of \$357,247. This amount is considered by the Company to be at fair market value.

ITEM 3. Legal Proceedings

The Company's insurance subsidiaries are subject to routine legal proceedings in connection with their property and casualty business. Penn-America has been named as a defendant in litigation commenced in the Superior Court of California, County of Los Angeles, on November 6, 2000 and in an identical suit on December 18, 2000 in the County of Orange relating to the Company's exited non-standard personal automobile business. Management believes that its position is defensible as to such litigation, but, the Company is pursuing settlement discussions at this time. Irrespective of Management's current activity, Management does not believe at this time that any settlement or judgment will have a material effect on the Company's financial statements. The Company is involved in no other pending or threatened legal or administrative proceedings which management believes might have a material adverse effect on the Company's financial condition or results of operations.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matter was submitted during 2001 to a vote of holders of PAGI's common stock.

Page 19

PART II

ITEM 5. Market for the Registrant's Common Stock and Related Stockholder Matters

Market and Common Stock Information

The Company's common stock trades on the New York Stock Exchange under the symbol "PNG". As of February 1, 2002 there were 190 registered holders of record and approximately 1,000 beneficial holders of record of the company's common stock. The high and low sale prices of the common stock were as follows:

	Market Price (1)	
	High	Low
Year Ended December 31, 2001		
First Quarter	\$ 6.97	\$4.79
Second Quarter	7.00	6.67
Third Quarter	6.80	6.40
Fourth Quarter	7.03	6.00
Year Ended December 31, 2000		
First Quarter	\$ 6.00	\$4.42

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Second Quarter	6.50	4.75
Third Quarter	5.25	4.59
Fourth Quarter	6.29	4.59

(1) Market prices are adjusted to reflect a three-for-two split of the Company's common stock effected on May 9, 2002.

Page 20

ITEM 6. SELECTED FINANCIAL DATA

Selected Financial Data

As described in Part I, the Company has restated its previously issued financial statements for the years ended December 31, 2001, 2000, and 1999. See Note 1 to consolidated financial statements for further information regarding the restatement.

	Year ended December 31,		
	2001	2000	1999
	(Restated)	(Restated)	(Restated)
	(dollars in thousand, except		
Operating Data:			
Premiums earned	\$ 88,934	\$ 91,449	\$ 85,677
Net investment income	11,339	10,454	9,537
Net realized investment gain (loss)	18	1,314	(1,178)
Total revenues	99,095	99,095	95,104
Net income (loss)	4,940	(4,831)	1,410
Comprehensive income (loss)	7,254	(343)	(5,000)
Diluted net income (loss) per share (1)	0.43	(0.42)	0.11
Cash dividends per share (1)	\$ 0.14	\$ 0.14	\$ 0.1383
Cash flow provided (used) by operations (2)	8,423	14,991	8,602
Insurance Performance Data			
Gross written premiums (3)	\$ 98,412	\$ 109,791	\$ 95,983
Net written premiums (4)	87,123	97,250	87,036
GAAP basis:			

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Loss ratio (5)	68.5	82.4	73.8
Expense ratio (6)	34.6	34.0	34.5
	-----	-----	-----
Combined ratio (7)	103.1	116.4	108.3

Balance Sheet Data (at the end of the period):

Cash and investments	\$ 188,615	\$ 178,675	\$ 166,227
Total assets	248,115	239,486	217,782
Total stockholders' equity	80,391	74,051	80,618
Total stockholders' equity per share (1)	7.00	6.52	6.67

Page 21

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Management's Discussion and Analysis of Financial Condition and Results of Operations

Penn-America Group, Inc. ("PAGI" or the "Company") has recently resolved various accounting and disclosure comments from the Securities and Exchange Commission ("SEC"), in conjunction with the Company's registration statement filing relating to the issuance of additional shares of common stock. One of the comments addressed the timing of recording other than temporary ("OTT") declines in the market value of certain equity securities. In order to resolve the comments, the Company agreed to amend its accounting policy and record OTT write-downs on these securities for the periods ending December 31, 2001, 2000 and 1999. This restatement affects net income for each of these periods but has no affect on stockholders' equity since the unrealized loss on these securities was already recorded in Accumulated Other Income (Loss) in the Consolidated Balance Sheets and Statements of Stockholders' Equity. The Company has restated its financial statements for the affected periods and has filed such restatements on this amended Form 10-K for the year ended December 31, 2001. For further information, see Note 1 of the Notes to Consolidated Financial Statements.

The affect of the restatement on total revenues, net income (loss), and basic and diluted net income (loss) per share are as follows:

				For the years ended	
December 31, 2001		December 31, 2000			
-----		-----			
As Reported	As Restated	As Reported	As Restated		
-----	-----	-----	-----		

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Total revenues	\$99,718	\$99,095	\$100,572	\$99,095
Net income (loss)	5,351	4,940	(3,856)	(4,831)
Net income (loss) per share				
Basic	0.47	0.43	(0.33)	(0.42)
Diluted	0.47	0.43	(0.33)	(0.42)

The OTT write-downs are non-cash items, and have no affect on stockholders' equity as the declines in market value on preferred and common stocks were previously recorded in stockholders' equity as net unrealized losses in accumulated other income (loss).

In addition, the SEC requested the Company add certain disclosures or not disclose certain information. This Management's Discussion and Analysis of Financial Condition and Results of Operations has been amended to respond to those requests.

The following discussion should be read in conjunction with the Company's Consolidated Financial Statements of the Company and Notes to the Consolidated Financial Statements.

General

Penn-America Group, Inc. ("PAGI") is a specialty property and casualty insurance holding company which, through its subsidiary, Penn-America Insurance Company and its subsidiary Penn-Star Insurance Company (collectively "Penn-America" or the "Company") markets and underwrites commercial property, general liability and multi-peril insurance for small businesses located primarily in small towns and suburban and rural areas. Penn-America can write business in all fifty states and the District of Columbia. The Company writes business on both an

Page 22

admitted and non-admitted (excess and surplus lines) basis in thirty-six states, on only an admitted basis in two states and on only a non-admitted basis in twelve states and the District of Columbia. The Company chooses in each state whether to write business on an admitted or non-admitted basis based upon the Company's analysis of competition in each state. Writing business on an admitted basis is highly regulated. The regulations, which vary by state, generally govern licensing, underwriting rules, rates and policy forms, and require insurance companies to pay premium taxes and guaranty fund assessments. Writing business on a non-admitted basis is significantly less regulated and provides much more freedom in setting rules, rates and policy forms and removes insurance companies from premium taxes and guaranty fund assessment liabilities. Coverage written on a non-admitted basis is less comprehensive than coverage issued on an admitted basis. If the Company chooses non-admitted status, the Company could be at a competitive disadvantage to carriers writing on an admitted basis if those competitors choose to offer coverages which are more comprehensive and attractive to an insured. Further, surplus lines agents are prohibited from writing non-admitted business in states in which they are not resident. Thus, if the Company does not have resident surplus lines agents in every state (currently, we do not in 7 states), the Company is precluded from writing business on a non-admitted basis in those states.

Penn-America's commercial insureds consist primarily of small, "Main Street" businesses including restaurants, mercantiles and non-residential service

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

contractors. In addition, the Company has developed customized products and coverages for other small commercial insureds such as day-care facilities, fitness centers and special events. The Company believes it has benefited from a general migration of small businesses out of urban centers and into suburban and rural areas. Industry consolidation, corporate downsizing and the increased use of communications technology and personal computers, among other factors, have contributed to the high growth in the number of small businesses in these areas. The Company selects only insurance lines of business and industry segments for which it can reasonably evaluate the probability of future loss exposure. Therefore, the Company avoids high-hazard risks and high-hazard lines of business such as medical malpractice and environmental liability.

Penn-America markets its products through fifty-seven high-quality general agents, who in turn produce business through more than 25,000 retail insurance brokers located throughout the United States. The Company focuses on serving the insurance needs of small businesses in small towns and rural areas that are serviced by retail insurance brokers with limited access to larger, standard lines insurers. The Company believes that larger, standard lines insurers, which often limit their underwriting to larger policies and to certain risk classes, generally underserve these markets. Penn-America believes that its distribution network enables it to effectively access these numerous small markets at a relatively low fixed-cost through the marketing, underwriting and administrative support of its general agents. This access also is enabled by the local market knowledge and expertise of its general agents and their retail insurance brokers.

Penn-America's distribution strategy is to maintain strong relationships with a select group of high-quality general agents. The Company carefully selects a limited number of general agents based on their experience and reputation and strives to preserve each agent's franchise value within its marketing territory. The Company seeks to grow with these general agents and to develop strong, long-standing relationships by providing a high level of service and support. The success of the Company's strategy is demonstrated by its strong and consistent growth. From 1992 to 2001, commercial gross written premiums grew at an 18% compound annual rate from \$22.6 million to \$98.4 million while the number of general agents rose from 38 to 57.

Page 23

Commercial Gross Written Premium
Per General Agent
(Same Store Sales)

(Dollars in millions)	1992	2001	Compound Annual Growth %
Commercial gross written premiums	\$ 22.6	\$98.4	18%
Number of general agents	38	57	5%

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Commercial gross written premiums per general agent	\$ 0.6	\$ 1.7	13%
---	--------	--------	-----

Core Commercial Business

The Company underwrites its core commercial business (excluding the Company's exited commercial automobile business - see Exited Lines, below) through three underwriting units: the Binding Authority Unit, the Submit Unit and the Specialty Lines Unit, which are defined as follows:

- o Binding authority business represents risks that may be quoted and bound by the Company's general agents prior to the Company's underwriting review.
- o Submit business represents risks that must be submitted by the Company's general agents to the Company prior to quoting or binding the account.
- o Specialty lines business represents risks that meet specific, pre-determined industry-segment and territorial parameters and may be quoted or bound by the Company's general agents prior to the Company's underwriting review.

The Binding Authority Unit accounted for approximately 88% of the Company's core commercial gross written premiums in 2001. Of this amount, approximately 85% is bound by general agents in accordance with the Company's underwriting manual. The Binding Authority Unit reviews, on a continuous basis, the new and renewal policies issued by the general agents to ensure that the Company's underwriting guidelines are followed. The Company provides its general agents with a comprehensive, regularly updated underwriting manual, which also is available online through a private intranet site called PennLINK. This manual clearly outlines the Company's risk eligibility, pricing, underwriting guidelines and policy issuance instructions. Penn-America closely monitors the underwriting quality of its business through on-line system edits and in-force account reviews. The Company also periodically audits each agent's office to determine if the Company's underwriting guidelines are followed in all aspects of risk selection, underwriting compliance, policy issuance and pricing. In addition to standard commissions, the Company provides strong incentives to its general agents to produce profitable business through a contingent profit commission structure that is tied directly to underwriting profitability. Payments of these contingent profit commissions have been through the issuance of shares of PAGI common stock and cash. Since 1996, the Company has awarded agents approximately 276,000 shares of PAGI common stock through its contingent profit commission structure.

Page 24

The Submit Unit was formed in 1999 in response to general agents who had risks similar to the Company's risk profile but were outside of their underwriting authority. The unit provides a market to the Company's general agents for approximately fifty classes of business. One hundred percent of the business is quoted and bound by Penn-America underwriters; general agents have no binding authority. This unit accounted for approximately 5% of core commercial gross written premiums in 2001.

The Specialty Lines Unit, which accounted for 7% of the Company's core

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

commercial gross written premiums in 2001, creates specialized underwriting and marketing programs for individual general agents based upon specific territorial needs and opportunities. The individual general agent typically is given exclusive marketing authority for the program subject to territorial limitations. The Company believes it can achieve superior underwriting results and expense savings on these programs. The Company continuously is developing specialized programs for certain industry segments to meet the needs of these insureds. For example, Penn-America has developed programs for cargo and Alaska dwellings. Collectively, these programs are a significant benefit to the Penn-America's marketing efforts.

Exited Lines

The Company offered commercial automobile coverage from 1998 through the first quarter of 2001. In late 2000, the Company announced that it was exiting this line of business due to unsatisfactory underwriting results. No new policies have been written since the first quarter of 2001 and all policies are being non-renewed. Gross written premiums for commercial automobile business decreased to \$1.1 million in 2001 from \$11.5 million in 2000 and \$7.0 million in 1999.

The Company exited non-standard personal automobile business in 1999 and, as a result, gross written premiums declined to \$2,000 in 2001 from \$2.8 million in 2000 and \$11.5 million in 1999.

Competition

The property and casualty insurance industry is highly competitive. Penn-America competes with domestic and international insurers, some of which have greater financial, marketing and management resources and experience than the Company. The Company also may compete with new market entrants in the future. Competition is based on many factors including the perceived market strength of the insurer, pricing and other terms and conditions, services provided, the speed of claims payment, the reputation and experience of the insurer and ratings assigned by independent rating organizations such as A.M. Best Company. Penn-America Insurance Company and Penn-Star Insurance Company currently have a pooled rating from A.M. Best of "A-" (Excellent). "A-" is the fourth highest of sixteen rating categories, and is considered "excellent" by A.M. Best Co. These ratings are based upon factors of concern to policyholders and are not directed toward the protection of investors.

Reinsurance

The Company purchases reinsurance in order to lower its retention for individual risks, enable it to underwrite policies with higher limits of liability and to protect against catastrophic losses. Reinsurance does not discharge the Company from its primary liability for the full amount of insured claims. The Company carefully examines the financial condition of its reinsurers and places its coverage only with financially sound companies.

Page 25

The Company has a multiple-line excess-of-loss reinsurance treaty currently in place that provides the following reinsurance coverage:

Line of Business

Company Policy Limit

Reinsurance Coverage / Company Retention

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Property	\$2.0 million per risk	\$1.7 million per risk in excess of \$
Commercial Automobile	\$1.0 million per occurrence	\$750,000 per occurrence in excess of occurrence
General Liability	\$3.0 million per occurrence	\$2.5 million per occurrence in excess of occurrence

Umbrella liability coverages are provided up to \$5.0 million per occurrence and are reinsured for 90% of policy limits up to \$1.0 million per occurrence and 100% of policy limits to \$4.0 million in excess of \$1.0 million per occurrence.

The Company may write individual policies with limits of liability greater than the aforementioned Company policy limits. These limits of liability are 100% reinsured on a facultative reinsurance basis.

The Company maintains a catastrophic loss reinsurance program the terms of which provide for 100% retention of the first \$1.0 million per occurrence, reinsurance of 90.0% of \$1.0 million per occurrence in excess of \$1.0 million per occurrence and reinsurance of 100% of \$23.0 million per occurrence in excess of \$2.0 million per occurrence.

Results of Operations

Year ended December 31, 2001 compared with year ended December 31, 2000

Gross written premiums decreased 10.4% to \$98.4 million for the year ended December 31, 2001 from \$109.8 million for the year ended December 31, 2000. The decrease was due to the decline of \$13.2 million in gross written premiums for the exited commercial and non-standard personal automobile lines. Core commercial gross written premiums increased 1.9% in 2001 to \$97.3 million from \$95.5 million in the prior year. This increase was attributable mainly to rate increases implemented during the year as well as growth in new business, which were offset partially by a decline in the renewal ratio due to the Company's decision to exit the residential contractors industry segment.

Ceded written premiums, the portion of gross premiums reinsured by other unaffiliated insurers, decreased to \$11.3 million for the year ended December 31, 2001 compared to \$12.5 million for the year ended December 31, 2000. The decline in ceded written premiums is primarily due to the decline in gross written premiums.

Net written premiums, which are gross written premiums less ceded written premiums, decreased 10.4% to \$87.1 million for the year ended December 31, 2001 from \$97.3 million for the year ended December 31, 2000. This decline is consistent with the drop in gross written premiums. Premiums earned decreased 2.8% to \$88.9 million for the year ended December 31, 2001 from \$91.5 million for the year ended December 31, 2000.

Net investment income increased 8.5% to \$11.3 million for the year ended December 31, 2001 from \$10.5 million for the year ended December 31, 2000. The increase resulted principally from an increase in the investment yield of the fixed-income investment portfolio and the growth in invested assets, partially offset by a decline in interest rates on overnight cash balances.

Net realized investment loss for the year ended December 31, 2001 was \$1.2 million for the year ended December 31, 2001 as compared with \$2.8 million for the year ended December 31, 2000. Net realized investment loss for the years

ended December 31, 2001 and 2000 included other-than-temporary impairment write-downs on certain of the Company's preferred and common stock investments of \$1.2 million and \$1.7 million, respectively.

For the year ended December 31, 2001, the other-than-temporary impairment write-down was primarily due to declines in the market value of two common stock exchange-traded funds, S & P 500 Depositary Receipts and Biotech Holders Trust, totaling \$1.0 million. For the year ended December 31, 2000, the other-than-temporary impairment write-downs were due to declines in the market value of twelve preferred stock securities totaling \$1.3 million and one common stock, AMEX Technology Fund, totaling \$0.4 million.

Losses and loss adjustment expenses decreased 19.2% to \$60.9 million in 2001 as compared with \$75.4 million in 2000. The 2000 operating results included strengthening of prior year loss reserves of \$9.2 million. This prior year reserve increase related principally to the commercial automobile liability, commercial multi-peril liability and other liability lines of business.

The September 11, 2001 tragedies in New York, Washington D.C. and Pennsylvania resulted in no property or casualty losses to the Company.

Amortization of deferred acquisition costs (ADAC) decreased 9.9% to \$22.7 million for the year ended December 31, 2001 from \$25.2 million for the year ended December 31, 2000. The decrease is due to lower commission rates to general agents that were implemented in the third quarter of 2000 and lower premium taxes as a result of the Company writing a larger portion of its business on a non-admitted basis. Also contributing to the decrease were lower commissions related to the exited lines of business. Non-standard personal automobile commission rates were higher than commercial rates.

Other underwriting and corporate expenses increased 29.2% to \$8.6 million for the year ended December 31, 2001 from \$6.6 million for the year ended December 31, 2000. This increase was due to the recording of additional expenses related to guarantee fund assessments and an increase in the allowance for doubtful accounts. Costs related to audits of assureds' records and salary expenses also were higher in 2001 than in the prior year.

The GAAP combined ratio, which is the sum of the loss and expense ratios, decreased to 103.1 for the year ended December 31, 2001 compared with 116.4 for the year ended December 31, 2000. The loss ratio, which is calculated by dividing losses and loss adjustment expenses by premiums earned, decreased to 68.5 for the year ended December 31, 2001 from 82.4 for the year ended December 31, 2000. As noted above, 2000 operating results included the strengthening of prior year loss reserves by \$9.2 million. This strengthening added approximately 10.0 points to the 2000 loss and combined ratios. The GAAP expense ratio, which is calculated by dividing the sum of ADAC and other underwriting expenses by premiums earned, for the year ended December 31, 2001, increased slightly to 34.6 from 34.0 for the year ended December 31, 2000. The GAAP combined ratio is a standard measure of underwriting profitability used throughout the property and casualty insurance industry. A ratio below 100.0 generally indicates profitable underwriting results.

As a result of the factors described above, net income for the year ended December 31, 2001 was \$4.9 million or \$0.43 per share (basic and diluted) as compared with a net loss of \$4.8 million or \$0.42 per share (basic and diluted) for the year ended December 31, 2000.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Year ended December 31, 2000, compared with year ended December 31, 1999

Gross written premiums increased 14.4% to \$109.8 million for the year ended December 31, 2000 from \$96.0 million for the year ended December 31, 1999. This increase resulted from a 26.7% increase in commercial lines gross written premiums to \$107.0 million, partially offset by a 75.8% decline in gross written premiums for the non-standard personal automobile lines of business to \$2.8 million. The Company exited the non-standard personal automobile lines of business in 1999.

Net written premiums increased 11.7% to \$97.3 million for the year ended December 31, 2000 from \$87.0 million for the year ended December 31, 1999. During the same period, net premiums earned increased 6.7% to \$91.5 million from \$85.7 million. The increase in net premiums earned corresponds to the increase in gross and net written premiums.

Net investment income increased 9.6% to \$10.5 million for the year ended December 31, 2000 from \$9.5 million for the year ended December 31, 1999. The increase resulted principally from an increase in yields on fixed-income investments and an increase in cash flows from operations due principally to the growth in written premiums and a reduction in paid losses.

Net realized investment loss for the year ended December 31, 2000 was \$2.8 million as compared with \$0.1 million for the year ended December 31, 1999. Realized investment losses were generated in 2000 due to our decision to sell selected securities and reinvest the proceeds into higher-yielding securities, along with other-than-temporary impairment write-downs due to declines in the market value of eleven preferred stock securities totaling \$1.3 million and one common stock, AMEX Technology Fund, totaling \$0.4 million.

Losses and loss adjustment expenses increased 19.3% to \$75.4 million in 2000 as compared with \$63.2 million in 1999. The 2000 operating results included strengthening of prior year loss reserves of \$9.2 million relating principally to our commercial automobile liability, commercial multi-peril liability and other liability lines of business. Operating results in 1999 included adverse loss development of \$8.4 million in our discontinued non-standard personal automobile, other liability and property lines of business. Property results in 1999 also were affected by losses related to Hurricanes Floyd and Irene and other windstorm damage.

Amortization of deferred acquisition costs (ADAC) increased 1.7% to \$25.2 million for the year ended December 31, 2000 from \$24.8 million for the year ended December 31, 1999. The increase was attributable primarily to the growth in premiums earned.

Other underwriting and corporate expenses increased 10.0% to \$6.6 million for the year ended December 31, 2000 from \$6.0 million for the year ended December 31, 1999. This increase was mainly attributable to increases in salary and benefit expenses.

The GAAP combined ratio increased to 116.4 for the year ended December 31, 2000 compared with 108.3 for the year ended December 31, 1999. The loss ratio increased to 82.4 for the year ended December 31, 2000 from 73.8 for the year ended December 31, 1999. The GAAP expense ratio decreased to 34.0 for the year ended December 31, 2000 from 34.5 for the year ended December 31, 1999.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

As a result of the factors described above, net loss for the year ended December 31, 2000 was \$4.8 million or \$0.42 per share (basic and diluted) as compared with net income of \$1.4 million or \$0.11 per share (basic and diluted) for the year ended December 31, 1999.

Critical Accounting Estimates and Policies

The Company is directly liable for losses and loss adjustment expenses under the terms of the insurance policies it writes. In many cases, several years may lapse between the occurrence of an insured loss, the reporting of the loss and the payment of that loss. The Company reflects its liability for the ultimate payment of all incurred losses and loss adjustment expenses by establishing loss and loss adjustment expense reserves as balance sheet liabilities for both reported and unreported claims.

When a claim involving a probable loss is reported, the Company establishes a case reserve for the estimated amount of its ultimate loss. The estimate of the amount of the ultimate loss is based upon factors such as:

- o the type of loss,
- o the jurisdiction of the occurrence,
- o the Company's knowledge of the circumstances surrounding the claim,
- o the severity of injury or damage,
- o the potential for ultimate exposure, and
- o policy provisions relating to the claim.

The Company determines loss adjustment expenses via a formula method that estimates loss adjustment expenses as a percentage of expected indemnity losses based on historical patterns adjusted to current experience.

In addition to case reserves, the Company establishes reserves on an aggregate basis to provide for incurred but not reported losses and loss adjustment expenses, commonly referred to as "IBNR". To establish reserves for IBNR, the Company must estimate the ultimate liability based primarily on past experience. The Company applies a variety of traditional actuarial techniques to estimate its ultimate liability. The techniques recognize, among other factors:

- o the Company's and the industry's experience,
- o historical trends in reserving patterns and loss payments,
- o the impact of claim inflation,
- o the pending level of unpaid claims,
- o the cost of claim settlements, o the line of business mix, and
- o the economic environment in which property and casualty insurance companies operate.

The Company continually reviews these estimates and, based on new developments and information, the Company includes adjustments of the probable ultimate liability in the operating results for the periods in which the adjustments are made. In general, initial reserves are based upon the actuarial and underwriting data utilized to set pricing levels and are reviewed as additional information, including claims experience, becomes available. The establishment of loss and loss adjustment expense reserves makes no provision for the broadening of coverage by legislative action or judicial interpretation or for the extraordinary future emergence of new types of losses not sufficiently represented in our historical experience, or which cannot yet be quantified. The Company regularly analyzes its reserves and reviews pricing and reserving

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

methodologies so that future adjustments to prior year reserves can be minimized. However, given the complexity of this process, reserves will require continual updates and the ultimate liability may be higher or lower than previously indicated. The Company does not discount its loss reserves.

The table below illustrates the sensitivity to a hypothetical change in the estimated net loss and loss adjustment expense reserves as of December 31, 2001. The selected scenarios are not predictions of future events, but rather illustrative of the effect that such events may have ultimate stockholders' equity.

(Dollars in thousands) Hypothetical change in net loss and loss adjustment expense reserve	Balance of Net Loss and Loss Adjustment Expense Reserves
-----	-----
3% adjustment - increase	\$96,867
2% adjustment - increase	95,927
1% adjustment - increase	94,986
No change	94,046
1% adjustment - decrease	93,106
2% adjustment - decrease	92,165
3% adjustment - decrease	91,225

Activity in the liability for unpaid losses and loss adjustment expenses is summarized as follows:

	Year ended December 31,		
	2001	2000	1999

	(in thousands)		
Balance, beginning of year	\$115,314	\$93,719	\$88,937
Less reinsurance recoverable	24,093	18,086	16,502
	-----	-----	-----
Net balance, beginning of year	91,221	75,633	72,435
Incurred related to:			
Current years	60,885	66,214	54,768
Prior years	36	9,164	8,419
	-----	-----	-----
Total incurred	60,921	75,378	63,187
Paid related to:			
Current year	19,913	26,273	23,540
Prior year	38,183	33,517	36,449
	-----	-----	-----
Total paid	58,096	59,790	59,989
Net balance, end of year	94,046	91,221	75,633
Plus reinsurance recoverable	25,552	24,093	18,086
	-----	-----	-----
Balance, end of year	\$119,598	\$115,314	\$93,719

=====

In 2001, the Company increased incurred losses and loss adjustment expenses attributable to insured events of prior years by \$36,000. This increase related entirely to the commercial automobile line of business. During 2001, the Company increased its estimate for the commercial multi-peril liability line of business by \$1.8 million due to the development of outstanding claim reserves on claims occurring primarily in 1998 and 1999. This increase was almost entirely offset by a reduction in the Company's estimate for the non-standard personal automobile line of business due to favorable settlements on closed claims.

In 2000, the Company increased incurred losses and loss adjustment expenses attributable to insured events of prior years by \$9,164,000. The increase is primarily attributable to changes in the Company's estimates for losses and loss

Page 30

adjustment expense reserves of \$1,400,000 for commercial automobile, \$3,900,000 for commercial multi-peril liability and \$3,400,000 for other liability lines of business.

The Company began writing commercial automobile coverage for vehicles and light trucks in 1998. The initial estimates for 1998 and 1999 were based on a relatively low level of claims reported to us. In 2000, the Company received a significant number of claims relating to accidents incurred in 1998 and 1999. In the fourth quarter of 2000, the Company exited the commercial automobile line of business due to unsatisfactory underwriting results.

The change in estimates in 2000 for the commercial multi-peril liability line of business resulted principally from increased exposure to liquor liability losses for policies primarily written in 1998 and 1999. In 2000, the Company revised its underwriting approach significantly to reduce its exposure to liquor liability.

The change in estimates in 2000 for the other liability line resulted principally from construction defect claims, which were new types of claims that were not anticipated when the Company wrote these policies between 1991 and 1996. These claims predominantly related to residential contractors and sub-contractors in California. In 2000, the Company completed its withdrawal from the residential contractors and sub-contractors industry segment.

In 1999, the Company increased incurred losses and loss adjustment expenses attributable to insured events of prior years by \$8,419,000. The increase is primarily attributable to changes in estimates for losses and loss adjustment expense reserves for non-standard personal automobile line of business. In 1999, the Company received a significant number of claims relating to accidents incurred prior to 1999, resulting in an increase in loss estimates. In 1999, the Company exited the non-standard personal automobile lines.

Incurred losses and loss adjustment expenses include estimates, recorded as loss and loss adjustment expense reserves on the balance sheet, for the ultimate payment on both reported and unreported claims. The Company changes its estimates for loss and loss adjustment expenses reserves as new events occur, as more loss experience is acquired or as additional information is received. Estimates for loss and loss adjustment expense reserves result from a continuous review process and the change in these estimates, as required by Financial Accounting Standards Board No. 60, Accounting and Reporting by Insurance Enterprises, paragraph 18, is recorded in the period that the change in these

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

estimates is made.

The Company believes that its loss and loss adjustment expense reserves are fairly stated as of December 31, 2001 due to the exiting of non-standard personal and commercial automobile lines of business and the reduction in exposure to construction defect and liquor liability losses. In addition, the Company implemented improvements in the loss reserving process, including the development of monthly and quarterly loss and loss adjustment expense reserve analyses and the creation of a reserve committee that meets quarterly.

The following table presents accident year loss and loss adjustment expense ratios (the sum of losses and loss adjustment expenses divided by premiums earned) for the ten most recent accident years (the year in which the loss occurred), as recorded as of December 31, 1999, 2000 and 2001 after giving effect to the increase in loss and loss adjustment expenses relating to changes in estimates of insured events of prior years. These "accident year" loss ratios differ from the loss ratios included in the Company's financial statements in

Page 31

that the latter loss ratios are based upon the year in which we recognize the loss for accounting purposes, regardless of when the loss actually occurred or was reported to the Company. See notes to consolidated financial statements in this report.

Accident Year	As of December 31,		
	1999	2000	2001
1992	69.6	72.1	72.5
1993	70.9	70.2	71.3
1994	69.1	72.0	71.8
1995	63.9	65.4	65.1
1996	68.1	68.3	69.4
1997	62.4	62.0	62.1
1998	63.6	65.8	65.0
1999	63.8	68.2	70.0
2000		72.4	70.2
2001			68.5

Liquidity and Capital Resources

PAGI is a holding company, the principal asset of which is the common stock of Penn-America Insurance Company. The principal source of cash to meet short-term liquidity needs, including the payment of PAGI dividends to stockholders and corporate expenses, is dividends from Penn-America Insurance Company. PAGI has no long-term debt obligations or planned capital expenditures that could impact PAGI's long-term liquidity needs. Penn-America Insurance Company's principal sources of funds are underwriting operations, investment income and proceeds from sales and redemptions of investments. Funds are used by Penn-America Insurance Company and Penn-Star Insurance Company principally to pay claims and operating expenses, to purchase investments and to make dividend payments to PAGI. PAGI's future liquidity is dependent on the ability of Penn-America Insurance Company to pay dividends to PAGI.

The Company's insurance subsidiaries are restricted by statute as to the amount of dividends that they may pay without the prior approval of regulatory

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

authorities. Penn-America Insurance Company may pay dividends to PAGI without advance regulatory approval only from unassigned surplus and only to the extent that all dividends in the past twelve months do not exceed the greater of 10% of total statutory policyholders' surplus, or statutory net income for the prior year. Using these criteria, the available ordinary dividend payable by Penn-America Insurance Company to PAGI for 2002 is \$6,473,325. No ordinary dividends have been paid to PAGI in 2002. Ordinary dividends paid by Penn-America Insurance Company to PAGI in 2001 were \$1.6 million. No ordinary dividends were paid to PAGI in 2000. Rather, after receiving approval from the Pennsylvania Insurance Department, Penn-America Insurance Company paid a \$6.4 million return of capital to PAGI in 2000, which PAGI used to repurchase common stock and to pay common stock dividends and PAGI operating expenses. Penn-America Insurance Company's ability to pay future dividends to PAGI without advance regulatory approval is dependent upon maintaining a positive level of unassigned and policyholders' surplus, which in turn, is dependent upon Penn-America Insurance Company and Penn-Star Insurance Company generating net income in excess of dividends to PAGI.

Penn-America Insurance Company and Penn-Star Insurance Company are required by law to maintain a certain minimum level of policyholders' surplus on a statutory basis. Policyholders' surplus is calculated by subtracting total liabilities from total assets. The National Association of Insurance Commissioners adopted risk based capital standards designed to identify property and casualty insurers that may be inadequately capitalized based on inherent risks of each insurer's assets and liabilities and its mix of net written premiums. Insurers falling below a calculated threshold may be subject to varying degrees of regulatory action. As of December 31, 2001, the policyholders' surplus of Penn-America Insurance Company and Penn-Star Insurance Company was in excess of the prescribed risk-based capital requirements. Penn-America Insurance Company's

Page 32

policyholders' surplus at December 31, 2001 was \$64,733,251 and its regulatory action level was \$17,124,648. Penn-Star Insurance Company's policyholders' surplus at December 31, 2001 was \$33,389,965 and its regulatory action level was \$5,675,459.

Net cash provided by operating activities decreased to \$8.4 million for the year ended December 31, 2001 from \$15.0 million for the year ended December 31, 2000. The decrease in net cash provided by operations resulted principally from the decrease in net written premiums during 2001, partially offset by a decrease in paid losses. Net cash used by investing activities was \$5.5 million for the year ended December 31, 2001, compared with \$9.1 million for the year ended December 31, 2000.

Net cash used by financing activities was \$1.2 million for the year ended December 31, 2001 as compared with \$6.5 million for the same period in 2000. In 2000, \$4.7 million was used by us to repurchase 858,638 shares of our common stock through a stock buy-back program, which was discontinued in the third quarter of 2000.

Investment Portfolio

The Company seeks to maintain sufficient liquidity from operations, investing and financing activities to meet its anticipated insurance obligations and operating and capital expenditure needs. The Company's investment strategy emphasizes quality, liquidity and diversification, as well as total return. With

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

respect to liquidity, the Company considers liability durations, specifically related to loss reserves, when determining desired investment maturities. In addition, maturities have been staggered to produce cash flows for loss payments and reinvestment opportunities. At December 31, 2001, the Company held a total of \$188.6 million in cash and investments. Of this amount, cash represented \$13.1 million, equity securities represented \$25.1 million, and fixed-income securities represented \$150.4 million.

The Company's cash and investments portfolio mix as December 31, 2001, was as follows:

Fixed income:

U.S. Treasury securities and obligations of U.S. government agencies	10%
Corporate securities	33%
Mortgage-backed securities	8%
Other structured securities	18%
Municipal securities	11%

Total fixed income	80%
Cash and short-term	7%
Preferred stock	9%
Common stock	4%

	100%
	=====

The Company's fixed-income portfolio of \$150.4 million was 80% of the total cash and investments as of December 31, 2001. Approximately 93% of these securities were rated "A" or better by Standard & Poor's. Standard & Poor's rates publicly traded securities in twenty categories ranging from AAA to CC. Securities with ratings from AAA to BBB- (the top ten categories) are commonly referred to as having an investment grade rating. Equity securities, the majority of which consist of preferred stocks and common stocks (comprised exclusively of exchange-traded funds), were \$25.1 million or 13% of total cash and investments as of December 31, 2001.

Page 33

As of December 31, 2001, the Company's investment portfolio contained corporate fixed-income and preferred stock securities with a market value of \$79.7 million. A summary of these securities by industry segment is as follows:

Financial institutions	48%
Communications	11%
Utilities	11%
Industrial	8%
Consumer, cyclical	6%
Basic materials	6%
Energy	4%
Technology	3%
Consumer, non-cyclical	3%

	100%
	=====

As of December 31, 2001, the Company's investment portfolio contained \$48.8

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

million of mortgage-backed, asset-backed and collateralized mortgage obligations. All of these securities were rated "AA-" or better and 75% were rated "AAA" by Standard & Poor's. These securities are publicly traded, and had market values obtained from an independent pricing service. Changes in estimated cash flows due to changes in prepayment assumptions from the original purchase assumptions are revised based on current interest rates and the economic environment. The Company had no derivative financial instruments, real estate or mortgages in the investment portfolio as of December 31, 2001. The quality of the fixed-income portfolio as of December 31, 2001, was as follows:

"AAA"	50%
"AA"	18%
"A"	25%
"BBB"	6%
Below "BBB"	1%

	100%
	=====

The Company regularly evaluates its investment portfolio to identify other-than-temporary impairments of individual securities. We consider many factors in determining if any other-than-temporary impairment exists, including the length of time and extent to which the market value of the security has been less than cost, the financial condition and near-term prospects of the issuer of the security and our ability and willingness to hold the security until the market value is expected to recover. The following table contains an analysis of the Company's securities with gross unrealized losses, categorized by the period that the securities were in a continuous unrealized loss position as of December 31, 2001:

Investment Securities with Gross Unrealized Losses, Categorized by Period of Continuous Unrealized Loss Position

(in thousands)	Number of Securities	Fair Value	Book Value	Gross Unrealized Losses	Six Months or Less
	-----	-----	-----	-----	-----
Fixed income securities	13	\$16,502	\$16,802	\$300	\$46
Preferred stock	1	1,005	1,053	48	
Common stock	3	1,888	2,018	130	9
				-----	-----
				\$478	\$55
				=====	=====

As of December 31, 2001, the Company's fixed-income investment portfolio had thirteen securities with \$300,000 of gross unrealized losses. No single issuer had an unrealized loss position greater than \$109,000. The over one year gross

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

unrealized losses for fixed income securities of \$71,000 represents 3 issuers rated A-, A- and BBB+ by Standard & Poor's, and the unrealized loss position was 2.3% of the securities' original cost. The over six months to one year gross unrealized losses for fixed income securities of \$183,000 primarily represents two public utility securities with maturity dates in 2004, were upgraded to B- and BB by Standard & Poor's in February 2002 and the unrealized loss position was 6% of the securities' original cost.

As of December 31, 2001, the Company's preferred stock portfolio had one security with a gross unrealized loss of \$48,000. This security is an investment grade security (Standard and Poor's rating "AA-") and the unrealized loss was 4.5% of its original cost.

As of December 31, 2001, the Company's common stock portfolio had three securities, all of which were exchange-traded funds, with \$130,000 of gross unrealized losses. No single issuer had an unrealized loss position of greater than \$80,000 or 11% of its book value.

Three-for-Two Stock Split

On April 11, 2002, the Company announced a three-for-two stock split to be effected in the form of a 50% stock dividend payable to stockholders of record as of April 25, 2002. The distribution date was May 9, 2002.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Market risk is the potential economic loss principally arising from adverse changes in the market value of financial instruments. The major components of market risk affecting us are interest rate risk and equity price risk.

Interest Rate Risk

The Company had fixed-income and preferred stock investments with a market value of \$167.7 million at December 31, 2001 that are subject to interest rate risk. The Company manages its exposure to interest rate risk through a disciplined asset/liability matching and capital management process. In the management of this risk, the characteristics of duration, credit and variability of cash flows are critical elements. These risks constantly are assessed and balanced within the context of the Company's liability and capital position.

The table below summarizes the Company's interest rate risk. The table illustrates the sensitivity of the market value of fixed-income and preferred stock investments to selected hypothetical changes in interest rates as of December 31, 2001. The selected scenarios are not predictions of future events, but rather illustrative of the effect that such events may have on the market value of the fixed-income and preferred stock portfolio and stockholders' equity.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Hypothetical Change in Interest Rates	Income and Preferred Stock Investments	Estimated Change in Market Value	----- Ma
	-----	-----	-----
200 basis point increase.	\$153,680	\$(14,062)	
100 basis point increase	160,460	(7,282)	
No change	167,742	---	
100 basis point decrease	175,463	7,721	
200 basis point decrease	183,532	15,790	

Equity Price Risk

Equity price risk is the Company's underlying exposure to an economic loss from the decline of common stock prices. The Company's common equity portfolio was \$8.0 million at December 31, 2001.

The Company attempts to mitigate equity price risk to its common stock portfolio by investing exclusively in exchange-traded funds, or ETFs. ETFs are securities that represent an interest in a trust that owns and holds a basket of common stocks that replicate a major market index (such as the S&P 500 or the Dow Jones Industrial Average) or a portion of a major market index (such as the Value Component of the S&P). Since these securities represent an interest in the equity capital markets as a whole, or a sub-sector thereof, they are a diversified, index-based exposure to common stocks. As such, the value of these ETFs will be determined by the performance of the equity capital markets in general or of a particular sub-sector and reduces equity price risk to a single issuer of stock.

The table below summarizes the Company's common equity price risk. The table illustrates the sensitivity of the market value of common stock investments to selected hypothetical changes in market prices as of December 31, 2001. The selected scenarios are not predictions of future events, but rather illustrative of the effect that such events may have on the fair value of the common stock investment portfolio and stockholders' equity.

(dollars in thousands)	Estimated Market Value of Common Equity Investments	Estimated Change in Market Value
Hypothetical Change in Market Price	-----	-----
20% price increase	\$9,572	\$1,595
10% price increase	8,775	798
No change	7,977	---
10% price decrease	7,179	(798)
20% price decrease	6,382	(1,595)

Impact of Inflation

Inflation can have a significant impact on property and casualty insurers because premium rates are established before the amounts of losses and loss adjustment expenses are known. The Company attempts to anticipate increases from inflation in establishing rates, subject to limitations imposed for competitive

pricing. The Company also considers inflation when estimating liabilities for losses and loss adjustment expenses, particularly for claims having a long period between occurrence and settlement. The liabilities for losses and loss adjustment expenses are management's best estimates of the ultimate net cost of underlying claims and expenses and are not discounted for the time value of

Page 36

money. In times of high inflation, the normally higher yields on investments may be offset partially by higher claims and expenses.

Cautionary Statements

Certain information included in management's discussion and analysis of financial condition and results of operations and elsewhere in this report are not historical facts but are forward-looking statements including, but not limited to, such matters as anticipated financial performance, business prospects, technological developments, new and existing products, expectations for market segment growth and similar matters. In connection with the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, the Company provides the following cautionary remarks regarding important factors which, among others, could cause the Company's actual results and experience to differ materially from the anticipated results or other expectations expressed in the Company's forward-looking statements. The risks and uncertainties that may affect the operations, performance, development, results of the Company's business and the other matters referred to above include, but are not limited to: (1) changes in the business environment in which the Company operates, including inflation and interest rates; (2) changes in taxes, governmental laws and regulations; (3) competitive product and pricing activity; and (4) difficulties of managing growth profitably. For additional disclosure regarding potential risk factors, please refer to the Company's 2001 10-K and other documents filed with the Securities and Exchange Commission.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Report of Independent Auditors

REPORT OF INDEPENDENT AUDITORS

The Board of Directors
Penn America Group, Inc.

We have audited the accompanying consolidated balance sheets of Penn-America Group, Inc. (the Company) as of December 31, 2001 and 2000, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2001. Our audit also included the financial statement schedules listed in Item 14(a) as of December 31, 2001 and for the year then ended. These financial statements and schedules are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedules based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1 to the consolidated financial statements, the Company has restated its 2001, 2000, and 1999 financial statements regarding the timing of recording other than temporary declines in the market value of certain equity securities.

In our opinion the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Penn-America Group, Inc. as restated at December 31, 2001 and 2000, and the consolidated results of its operations and its cash flows as restated for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States. Also, in our opinion, the related financial statement schedules, when considered in relation to the basic financial statements taken as a whole, present fairly, in all material respects, the information set forth therein.

Philadelphia, Pennsylvania
January 18, 2002
except for share and per share
information in Notes 2, 11, 14
and 15, the section entitled
"restatement of financial information"
in Note 1, the 7th and 13th paragraphs
in Note 1, all information marked
"restated" in the notes to consolidated
financial statements, the first paragraph
in Note 3, the next-to-last paragraphs in Note 4
and Note 8, and the last paragraph in Note 6,
as to which the date is November 1, 2002

Penn-America Group, Inc. and Subsidiaries
Consolidated Balance Sheets

(In thousands, except for per share data)

Assets

Investments:

Fixed maturities:

Available for sale, at fair value (amortized cost 2001, \$130,976; 2000, \$123,873) \$135,

Held to maturity, at amortized cost (fair value 2001, \$15,317; 2000, \$17,441) 15,

Equity securities, at fair value (cost 2001, \$24,720; 2000, \$24,895) 25,

Total investments 175,

Cash 13,

Accrued investment income 2,

Premiums receivable (net of allowances of \$972 in 2001 and \$422 in 2000) 12,

Reinsurance recoverable 25,

Prepaid reinsurance premiums 4,

Deferred policy acquisition costs 9,

Capital lease, affiliate 1,

Deferred income taxes 3,

Income tax recoverable

Other assets

Total assets \$248,

Liabilities and Stockholders' Equity

Liabilities:

Unpaid losses and loss adjustment expenses \$119,

Unearned premiums 41,

Accounts payable and accrued expenses 3,

Capitalized lease obligation, affiliate 1,

Other liabilities 1,

Total liabilities 167,

Stockholders' equity:

Preferred stock, \$.01 par value; authorized 2,000,000 shares;

None issued

Common stock, \$.01 par value; authorized 20,000,000 shares;

issued 2001 and 2000, 15,228,351 and 15,114,038 shares, respectively;

outstanding 2001 and 2000, 11,478,351 and 11,364,038 shares, respectively

Additional paid-in capital 70,

Accumulated other comprehensive income 3,

Retained earnings 31,

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Treasury stock, 3,750,000 shares, at cost	(24,1
Officers' stock loans	(6
Unearned compensation from restricted stock awards	(1

Total stockholders' equity	80,

Total liabilities and stockholders' equity	\$248,
	=====

See accompanying notes to Consolidated Financial Statements

Page 39

Penn-America Group, Inc. and Subsidiaries
Consolidated Statements of Operations

(In thousands, except per share data)	Year ended December	
	2001	2000
	(Restated)	(Restated)
Revenues		
Premiums earned	\$ 88,934	\$ 91,449
Net investment income	11,339	10,454
Net realized investment loss	(1,178)	(2,808)
Total revenues	99,095	99,095
Losses and expenses		
Losses and loss adjustment expenses	60,921	75,378
Amortization of deferred policy acquisition costs	22,715	25,219
Other underwriting expenses	8,030	5,850
Corporate expenses	548	791
Interest expense	160	161
Total losses and expenses	92,374	107,399
Income (loss) before income tax	6,721	(8,304)
Income tax expense (benefit)	1,781	(3,473)
Net income (loss)	\$ 4,940	\$ (4,831)
Net income (loss) per share		
Basic	\$ 0.43	\$ (0.42)
Diluted	\$ 0.43	\$ (0.42)

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Weighted average shares outstanding		
Basic	11,420,213	11,518,968
Diluted	11,501,703	11,518,968
Cash dividend per share	\$ 0.14	\$ 0.14

See accompanying notes to Consolidated Financial Statements

Page 40

Penn-America Group, Inc. and Subsidiaries
Consolidated Statements of Stockholders' Equity

(In thousands, except per share amounts)	Common Stock	Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)
			(Restated)
Balance at December 31, 1998	\$ 149	\$ 68,985	\$ 2,714
Net income	--	--	--
Other comprehensive loss:			
Unrealized loss on investments, net of tax and reclassification adjustment	--	--	(6,410)
Comprehensive loss			
Issuance of common stock	1	556	--
Unearned compensation from restricted stock awards issued	--	--	--
Amortization of compensation expense from restricted stock awards issued	--	--	--
Cash dividends paid (\$0.1383 per share)	--	--	--
Purchase of treasury stock, at cost	--	--	--
Balance at December 31, 1999	\$ 150	\$ 69,541	\$ (3,696)
Net loss	--	--	--
Other comprehensive income:			
Unrealized gains on investments, net of tax and reclassification adjustment	--	--	4,488
Comprehensive loss			
Issuance of common stock	1	573	--
Officers' stock loans	--	--	--
Unearned compensation from restricted stock awards issued	--	--	--
Amortization of compensation expense from restricted stock awards issued	--	--	--
Cash dividends paid (\$0.14 per share)	--	--	--
Purchase of treasury stock, at cost	--	--	--
Balance at December 31, 2000	\$ 151	\$ 70,114	\$ 792

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Net income	--	--	--
Other comprehensive income:			
Unrealized gains on investments, net of tax and reclassification adjustment	--	--	2,314
Comprehensive income			
Issuance of common stock	1	621	--
Officers' stock loans	--	--	--
Forfeiture of restricted stock awards	--	--	--
Amortization of compensation expense from restricted stock awards issued	--	--	--
Cash dividends paid (\$0.14 per share)	--	--	--
	-----	-----	-----
Balance at December 31, 2001	\$ 152	\$ 70,735	\$ 3,106
	=====	=====	=====

(In thousands, except per share amounts)	Officers' Stock Loans	Unearned Compensation From Restricted Stock Awards	Stock
Balance at December 31, 1998	\$ 0	\$ (354)	\$
Net income	--	--	
Other comprehensive loss:			
Unrealized loss on investments, net of tax and reclassification adjustment	--	--	
Comprehensive loss			
Issuance of common stock	--	--	
Unearned compensation from restricted stock awards issued	--	(91)	
Amortization of compensation expense from restricted stock awards issued	--	120	
Cash dividends paid (\$0.1383 per share)	--	--	
Purchase of treasury stock, at cost	--	--	
	-----	-----	-----
Balance at December 31, 1999	\$ 0	\$ (325)	\$
Net loss	--	--	
Other comprehensive income:			
Unrealized gains on investments, net of tax and reclassification adjustment	--	--	
Comprehensive loss			
Issuance of common stock	--	--	
Officers' stock loans	(546)	--	
Unearned compensation from restricted stock awards issued	--	(74)	
Amortization of compensation expense from restricted stock awards issued	--	120	
Cash dividends paid (\$0.14 per share)	--	--	
Purchase of treasury stock, at cost	--	--	
	-----	-----	-----
Balance at December 31, 2000	\$ (546)	\$ (279)	\$

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Net income	-----	-----	-----
	--	--	
Other comprehensive income:			
Unrealized gains on investments, net of tax and reclassification adjustment	--	--	
Comprehensive income	7,254		
Issuance of common stock	--	--	
Officers' stock loans	(83)	--	
Forfeiture of restricted stock awards	--	32	
Amortization of compensation expense from restricted stock awards issued	--	115	
Cash dividends paid (\$0.14 per share)	--	--	
	-----	-----	-----
Balance at December 31, 2001	\$ (629)	\$ (132)	\$
	=====	=====	=====

See accompanying notes to Consolidated Financial Statements

Page 41

Penn-America Group, Inc. and Subsidiaries
Consolidated Statements of Cash Flows

(In thousands)	Year ----- 2001 -----
	(Restated)
Cash flows from operating activities:	
Net income (loss)	\$ 4,940
Adjustments to reconcile net income (loss) to net cash provided by operating activities:	
Bond amortization (accretion) and depreciation expense, net	(5)
Net realized investment loss	1,178
Deferred income tax benefit	(711)
Net (increase) decrease in premiums receivable, prepaid reinsurance premiums and unearned premiums	(4,401)
Net increase in unpaid losses and loss adjustment expenses and reinsurance recoverable	2,927
Accrued investment income	(18)
Deferred policy acquisition costs	1,234
Income tax recoverable	2,915
Other assets	23
Accounts payable and accrued expenses	1,447
Other liabilities	(1,106)

Net cash provided by operating activities	8,423

Cash flows from investing activities:	
Purchases of equity securities	(4,162)
Purchases of fixed maturities available for sale	(28,672)

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Purchases of fixed maturities held to maturity	--
Proceeds from sales of equity securities	3,146
Proceeds from sales of fixed maturities available for sale	21,911
Proceeds from maturities of fixed maturities available for sale	--
Proceeds from maturities and calls of fixed maturities held to maturity	2,250
Change in short-term investments	--

Net cash used by investing activities	(5,527)

Cash flows from financing activities:	
Issuance of common stock	622
Purchase of treasury stock	--
Officers' stock loans	(83)
Principal payments on capital lease obligations, affiliate	(131)
Dividends paid	(1,600)

Net cash used by financing activities	(1,192)

Increase (decrease) in cash	1,704
Cash, beginning of period	11,425

Cash, end of period	\$ 13,129
	=====
Supplemental disclosure of cash flow information:	
Interest paid, affiliate	\$ 160
Taxes (recovered) paid	(492)

See accompanying notes to Consolidated Financial Statements

Page 42

Penn-America Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements

Note 1 Summary of Significant Accounting Policies

Basis of Presentation and Description of Business

Penn-America Group, Inc. ("PAGI") is an insurance holding company. Penn Independent Corporation ("Penn Independent") owned approximately 40% of the outstanding common stock of PAGI at December 31, 2001. The accompanying financial statements include the accounts of PAGI and its wholly owned subsidiary, Penn-America Insurance Company ("Penn-America") and its wholly owned subsidiary Penn-Star Insurance Company ("Penn-Star"), (collectively the "Company"). All significant inter-company accounts and transactions have been eliminated in consolidation. These financial statements are prepared in conformity with accounting principles generally accepted in the United States, which differ in some respects from those required by insurance regulatory authorities.

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

reporting period. Actual results could differ from those estimates.

The Company underwrites commercial property and general liability insurance and multi-peril insurance for small businesses located primarily in small towns and suburban and rural areas. The Company can write business in all fifty states and the District of Columbia. The Company writes business on both an admitted and non-admitted basis in thirty-six states, on only an admitted basis in two states and on only a non-admitted basis in twelve states and the District of Columbia.

Restatement of Financial Information

In conjunction with the Company's registration statement filing relating to the issuance of additional shares of common stock, the Company has resolved various accounting and disclosure comments from the Securities and Exchange Commission ("SEC"). One of the comments addressed the timing of recording other than temporary ("OTT") declines in the market value of certain equity securities. In order to resolve the comment, the Company agreed to amend its accounting policy and record OTT write-downs on these securities for the periods ending December 31, 2001, 2000, and 1999. This restatement affects net income for each of these periods but has no effect on stockholders' equity since the unrealized loss on these securities was already recorded in Accumulated Other Income (Loss) in the Consolidated Balance Sheets and Statements of Stockholders' Equity. By means of this filing, the Company is restating its previously issued financial statements for the years ended December 31, 2001, 2000, and 1999.

Below is a table showing a comparison of previously reported and restated total revenues, net income and net income per share (basic and diluted) for the periods affected.

	For the years ended,			
	December 31, 2001		December 31, 2000	
	As Reported	As Restated	As Reported	As Restated
Total revenues	\$99,718	\$99,095	\$100,572	\$99,095
Net income (loss)	5,351	4,940	(3,856)	(4,831)
Net income (loss) per share				
Basic	0.47	0.43	(0.33)	(0.42)
Diluted	0.47	0.43	(0.33)	(0.42)

Page 43

Penn-America Group, Inc. and Subsidiaries Notes to Consolidated Financial Statements - (Continued)

In addition, the SEC requested that the Company add certain disclosures. The consolidated financial statements have been amended as appropriate to respond to these requests.

Revenue Recognition

Premiums written are recognized as earned ratably over the terms of the respective policies and include estimates for premiums earned but not yet billed

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

of \$1,185,000 and \$0 as of December 31, 2001, and 2000, respectively. Unearned premiums represent the portion of premiums written applicable to the unexpired terms of policies in force and are calculated on a semi-monthly pro-rata basis.

Valuation of Premiums Receivable

The Company evaluates the collectibility of premiums receivable based on a combination of factors. In circumstances in which the Company is aware of a specific customer's inability to meet its financial obligations to the Company, a specific reserve for bad debts against amounts due is recorded to reduce the net receivable to the amount reasonably believed to be collectible. No such instances occurred in 2001. For all remaining balances, reserves are recognized for bad debts based on the length of time the receivables are past due based on historical statistics.

Investments

At the time of purchase of fixed-maturity investments, management makes a determination as to the investment classification ("Available for Sale" or "Held to Maturity"). Factors taken into consideration by management in determining the appropriate investment category are: maturity, yield, cash flow requirements and anticipated changes in interest rates. Fixed maturities classified as "Available for Sale" are carried at fair value with unrealized investment gains or losses, net of deferred income taxes, included as a separate component of accumulated other comprehensive income in stockholders' equity. "Held to Maturity" investments are carried at amortized cost.

Investments in fixed-maturity securities are adjusted for amortization of premium and accretion of discounts to maturity date using the interest method. Interest income is recognized on the accrual basis.

The amortized cost of mortgage-backed and asset-backed securities is calculated using the interest method including consideration of anticipated prepayments at the date of purchase. Significant changes in estimated cash flows from the original assumptions are accounted for using the composite method.

Equity securities are carried at fair value with the change in unrealized investment gains or losses, net of deferred income taxes, included as a separate component of accumulated other comprehensive income in stockholders' equity.

Realized gains or losses represent the difference between the book value of securities sold and the proceeds realized upon sale. The Company uses the specific identification method to determine the cost of securities sold. The cost of securities is adjusted where appropriate to include a provision for a decline in value that is considered to be other-than-temporary. The Company considers four factors in determining if an other-than-temporary decline exists: length of time and extent that a security has been in an unrealized loss position; the existence of an event that would impair the issuer's future earnings potential; the near term prospects for recovery of the market value of a security; and the intent and ability of the Company to hold the security until the market value recovers. Realized gains or losses, including any provision for other-than-temporary declines in value, are included in the statement of operations.

Policy Acquisition Costs

Policy acquisition costs such as commissions, salaries, premium taxes and

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

certain other underwriting expenses, which vary with and are directly related to the production of business, are deferred and amortized over the effective periods of the related insurance policies. The method followed in computing deferred policy acquisition costs limits the amount of such deferred costs to their estimated realizable values, which gives effect to the premium to be earned, related investment income, losses and loss adjustment expenses and certain other costs expected to be incurred as the premium is earned.

Losses and Loss Adjustment Expenses

The liability for losses and loss adjustment expenses represents estimates of amounts needed to pay reported and unreported claims and related expenses. These estimates are based on certain actuarial and other assumptions related to the ultimate cost to pay such claims. All estimates are reviewed periodically and as experience develops and new information becomes known, the reserves are adjusted as necessary. Such adjustments are reflected in the results of operations in the period in which they are determined.

Fair Values of Financial Instruments

The Company uses the following methods or assumptions in determining fair values:

Investment Securities: Fair values are based on quoted market prices or on quoted market prices of comparable instruments or values obtained from independent pricing services.

Premium and Reinsurance Receivables and Payables: The carrying amounts reported in the balance sheet for these instruments approximate their fair values.

Capitalized Lease Obligation: Fair value is based upon the present value of the underlying cash flows discounted at the Company's incremental borrowing rate at year-end. The carrying amounts reported in the balance sheet approximate fair value.

Reinsurance

In the ordinary course of business, the Company reinsures certain risks, generally on an excess-of-loss basis, with other insurance companies which principally are rated "A" or higher by A.M. Best. Such reinsurance arrangements serve to limit the Company's maximum loss. Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liabilities arising from the reinsured policies and incurred but not reported losses.

Capitalized Lease

The capitalized lease is carried at cost less accumulated amortization. Amortization is calculated using the interest method over 20 years, which represents the term of the mortgage on the office space that the Company rents from a related party.

Income Tax

Deferred income taxes are accounted for under the liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Penn-America Group, Inc. and Subsidiaries Notes to Consolidated
Financial Statements - (Continued)

Comprehensive Income (Loss)

Comprehensive income (loss) encompasses all changes in stockholders' equity (except those arising from transactions with stockholders) and includes net income and net unrealized investment gains and losses on fixed-income investments classified as "available-for-sale" and equity securities, net of deferred income tax.

Reclassification

Certain prior-year amounts have been reclassified to conform to 2001 classifications.

Note 2 Income Per Share

Basic net income (loss) per share is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding for each period. Diluted net income (loss) per share includes the potential dilution that could occur if the contracts to issue common stock were exercised and converted into common stock.

The following is a reconciliation of the basic and diluted net income (loss) per share computations:

	Year ended December 31,	
(In thousands, except per share data)	2001	2000
	(Restated)	(Restated)
Basic per share computation:		
Net income (loss)	\$ 4,940	\$ (4,831)
Weighted average common shares outstanding	11,420,213	11,518,968
Basic net income (loss) per share	\$ 0.43	\$ (0.42)
Diluted per share computation:		
Net income (loss)	\$ 4,940	\$ (4,831)
Weighted average common shares outstanding	11,420,213	11,518,968
Additional shares outstanding after the assumed exercise of options by applying the treasury stock method	81,490	*
Total shares	11,501,703	11,518,968
Diluted net income (loss) per share	\$ 0.43	\$ (0.42)

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

* As of December 31, 2000, the Company issued options to purchase 538,875 shares of common stock to employees and directors at prices ranging from \$3.61 to \$12.67. These options were not considered in the 2000 computation, as the impact was anti-dilutive.

Page 46

Penn-America Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements - (Continued)

Note 3 Transactions with Affiliates

Penn-America was formed by Irvin Saltzman, chairman of PAGI's board of directors and a director of Penn Independent. Jon S. Saltzman, Irvin Saltzman's son, is President and Chief Executive Officer of PAGI and a director of Penn Independent. The Saltzman family, substantially through their ownership of Penn Independent, owns approximately 40% of the outstanding common stock of PAGI at December 31, 2001.

Penn-America leases its home office facility from Irvin Saltzman and the lease is accounted for as a capital lease. The amount of property capitalized of \$2,227,000 is presented net of accumulated amortization of \$561,000 and \$474,000 as of December 31, 2001 and 2000, respectively. Capitalized lease obligations of \$1,570,000 and \$1,701,000 were recorded at December 31, 2001 and 2000, respectively, representing the lease obligation arising from this lease, which carries an 8.5% interest rate. Penn Independent and its subsidiaries also lease a portion of the building in which the Company's home office facility is located. Management believes that the lease terms are at market rates.

At December 31, 2001, the future minimum lease payments for the capitalized lease obligation are \$281,000 per year in 2002 through 2006 and the total minimum lease payments are \$2,262,000, of which \$692,000 is the amount representing interest.

Penn Independent provides the Company with human resource management and other services. The Company paid \$212,000, \$200,000 and \$200,000 in 2001, 2000 and 1999, respectively, for such services. Such amounts are based on allocations of estimated costs. All costs incurred by Penn Independent on behalf of the Company have been allocated to the Company and are reflected in the financial statements. Management believes that the methods used to allocate such costs are reasonable and that the Company's expenses on a stand-alone basis would not be materially different.

Gross written premiums with insurance agency affiliates of Penn Independent were \$3,888,000, \$3,282,000 and \$1,732,000 in 2001, 2000 and 1999, respectively. Commissions paid to such affiliates were \$857,000, \$740,000 and \$441,000 in 2001, 2000 and 1999 respectively. Premiums receivable includes receivable from affiliates of \$454,000 and \$535,000 as of December 31, 2001 and 2000, respectively.

Penn-America Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements - (Continued)

Note 4 Investments

The Company invests primarily in investment-grade fixed maturities, substantially all of which are rated "A" or higher by Standard & Poor's. The cost, gross unrealized gains and losses and fair values of investments are as follows:

(In thousands)	December 31, 2001		
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses
	(Restated)	(Restated)	(Restated)
Fixed maturities:			
Available for sale:			
U.S. Treasury securities and obligations of U.S. government agencies	4,013	\$ 182	\$ --
Corporate securities	49,981	2,091	51
Mortgage-backed securities	26,483	863	30
Other structured securities	20,758	725	21
Municipal securities	20,569	457	22
Public utilities	9,172	259	176
Total available for sale	130,976	4,577	300
Held to maturity:			
U.S. Treasury securities and obligations of U.S. government agencies	13,812	213	--
Corporate securities	276	14	--

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Public utilities	996	6	--
Total held to maturity	15,084	233	--
Total fixed-maturity securities	146,060	4,810	300
Equity securities	24,720	607	178
Total investments	\$170,780	\$ 5,417	\$ 478

Page 48

Penn-America Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements - (Continued)

(In thousands)	December 31, 2000		
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses
	(Restated)	(Restated)	(Restated)
Fixed maturities:			
Available for sale:			
U.S. Treasury securities and obligations of U.S. government agencies	\$ 4,015	\$ 107	\$ --
Corporate securities	52,084	668	387
Mortgage-backed securities	23,321	629	6
Other structured securities	21,381	497	6
Municipal securities	15,882	537	--
Public utilities	7,190	44	479
Total available for sale	123,873	2,482	878
Held to maturity:			
U.S. Treasury securities and obligations of U.S. government agencies	13,760	162	14
Corporate securities	2,378	--	4
Municipal securities	150	--	--

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Public utilities	994	15	--
Total held to maturity	17,282	177	18
Total fixed-maturity securities	141,155	2,659	896
Equity securities	24,895	454	858
Total investments	\$166,050	\$ 3,113	\$ 1,754

Fixed maturities at December 31, 2001, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or to prepay obligations with or without call or prepayment penalties.

(In thousands)	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	\$ 3,055	\$ 3,132	\$ 12,118	
Due after one year through five years	45,659	47,565	2,966	
Due after five years through ten years	27,198	27,585	-	
Due after ten years	7,823	8,193	-	
Mortgage-backed and other structured securities	47,241	48,778	-	
Total	\$ 130,976	\$ 135,253	\$ 15,084	

Page 49

Penn-America Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements - (Continued)

A summary of net investment income is as follows:

(In thousands)	Year ended December 31,		
	2001	2000	1999

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Interest on fixed maturities	\$ 9,835	\$ 8,508	\$ 7,629
Dividends on equity securities	1,421	1,422	1,492
Interest on short-term investments and cash	377	815	787
Other	37	26	4
	-----	-----	-----
Total investment income	11,670	10,771	9,912
Less investment expense	(331)	(317)	(375)
	-----	-----	-----
Net investment income	\$ 11,339	\$ 10,454	\$ 9,537
	-----	-----	-----

All investments in fixed-maturity securities were income-producing during 2001, 2000 and 1999. Realized pre-tax gains (losses) on the sale of investments are as follows:

(In thousands)	Year ended December 31,		
	2001	2000	1999
	(Restated)	(Restated)	(Restated)
Fixed maturities:			
Gross realized gains	\$ 218	\$ 24	\$ 66
Gross realized losses	(203)	(1,461)	(23)
	-----	-----	-----
Net realized investment gain (loss)	15	(1,437)	43
Equity securities:			
Gross realized gains	240	1,128	1,266
Gross realized losses	(1,433)	(2,499)	(1,419)
	-----	-----	-----
Net realized investment loss	(1,193)	(1,371)	(153)
	-----	-----	-----
Total net realized investment loss	\$ (1,178)	\$ (2,808)	\$ (110)
	-----	-----	-----

Income tax benefit on net realized losses was \$400,000, \$955,000 and \$38,000 in 2001, 2000, and 1999, respectively. Gross realized losses on equity securities for the year ended December 31, 2001, 2000 and 1999, included an other-than-temporary impairment write-down of \$1,226,000, \$1,770,000, and \$951,000, respectively.

The amortized cost of fixed maturities on deposit with various regulatory authorities at December 31, 2001 and 2000 amounted to \$10,998,000 and \$10,992,000, respectively.

Note 5 Reinsurance

In the normal course of business, the Company seeks to reduce the losses that may arise from catastrophes or other events that cause unfavorable underwriting results by reinsuring certain levels of risks in various areas of exposure with other insurance enterprises or reinsurers. Reinsurance contracts do not relieve the Company of its obligations to policyholders. Failure of reinsurers to honor their obligations could result in losses to the Company. Allowances have been established for amounts deemed uncollectible. The Company evaluates the financial condition of its reinsurers and monitors concentrations of credit risk arising from similar geographic regions, activities or economic characteristics

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

of the reinsurers to minimize its exposure to significant losses

Page 50

Penn-America Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements - (Continued)

from reinsurer insolvencies. At December 31, 2001, reinsurance recoverable and prepaid reinsurance premiums associated with two major reinsurers, General Reinsurance Corporation and American Reinsurance Corporation, were \$24.3 million and \$5.0 million, respectively.

Written premiums and premiums earned consisted of the following:

(In thousands)	Year ended December 31,		
	2001	2000	1999
Written premiums:			
Gross	\$ 98,412	\$ 109,791	\$ 95,791
Ceded	11,289	12,541	8,541
Net of reinsurance	\$ 87,123	\$ 97,250	\$ 87,250
Premiums earned:			
Gross	\$ 100,617	\$ 102,883	\$ 93,883
Ceded	11,683	11,434	8,434
Net of reinsurance	\$ 88,934	\$ 91,449	\$ 85,449

Loss and loss adjustment expenses are net of recoveries recognized under reinsurance contracts as follows: \$7,446,000, \$9,438,000 and \$7,182,000 in 2001, 2000 and 1999, respectively.

Note 6 Unpaid Losses and Loss Adjustment Expenses

Activity in the liability for unpaid losses and loss adjustment expenses is summarized as follows:

(In thousands)	Year ended December 31,		
	2001	2000	1999
Balance, beginning of year	\$ 115,314	\$ 93,719	\$ 83,719
Less reinsurance recoverable	24,093	18,086	18,086
Net balance, beginning of year	\$ 91,221	\$ 75,633	\$ 65,633

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Incurred related to:	91,221	75,633	7
Current year	60,885	66,214	5
Prior years	36	9,164	
Total incurred	60,921	75,378	6
Paid related to:			
Current year	19,913	26,273	2
Prior years	38,183	33,517	3
Total paid	58,096	59,790	5
Net balance, end of year	94,046	91,221	7
Plus reinsurance recoverable	25,552	24,093	1
Balance, end of year	\$ 119,598	\$ 115,314	\$ 9

Page 51

Penn-America Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements - (Continued)

In 2001, the Company increased incurred losses and loss adjustment expenses attributable to insured events of prior years by \$36,000. This increase related entirely to the commercial automobile line of business. During 2001, the Company increased its estimate for the commercial multi-peril liability line of business by \$1.8 million due to the development of outstanding claim reserves on claims occurring primarily in 1998 and 1999. This increase was almost entirely offset by a reduction in the Company's estimate for the non-standard personal automobile line of business due to favorable settlements on closed claims.

In 2000, the Company increased incurred losses and loss adjustment expenses attributable to insured events of prior years by \$9,164,000. The increase is primarily attributable to changes in the Company's estimates for losses and loss adjustment expense reserves of \$1.4 million for commercial automobile, \$3.9 million for commercial multi-peril liability and \$3.4 million for other liability lines of business. The Company began writing commercial automobile coverage for vehicles and light trucks in 1998. The Company's initial estimates for 1998 and 1999 were based on a relatively low level of claims reported. In 2000, the Company received a significant number of claims relating to accidents incurred in 1998 and 1999. In the fourth quarter of 2000, the Company exited the commercial automobile line of business due to unsatisfactory underwriting results. The Company's change in estimates in 2000 for the commercial multi-peril liability line of business resulted principally from its increased exposure to liquor liability losses for policies primarily written in 1998 and 1999. In 2000, the Company revised its underwriting approach significantly to

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

reduce its exposure to liquor liability claims. The Company's change in estimates in 2000 for the other liability line resulted principally from construction defect claims, which were new claims that were not anticipated by the Company when the Company wrote these policies between 1991 and 1996. These claims predominantly related to residential contractors and sub-contractors in California. In 2000, the Company completed its withdrawal from the residential contractors and sub-contractors industry segment.

In 1999, the Company increased incurred losses and loss adjustment expenses attributable to insured events of prior years by \$8,419,000. The increase is primarily attributable to changes in estimates for losses and loss adjustment expense reserves for our non-standard personal automobile line of business. For 1999, the Company received a significant number of claims relating to accidents incurred prior to 1999, resulting in an increase in the Company's loss estimates. For 1999, the Company exited the nonstandard personal automobile lines. Incurred losses and loss adjustment expenses include estimates, recorded as loss and loss adjustment expense reserves on the balance sheet, for the ultimate payment on both reported and unreported claims. The Company changes its estimates for loss and loss adjustment expenses reserves as new events occur, as more loss experience is acquired, or as additional information is received. The Company's estimates for loss and loss adjustment expense reserves result from a continuous review process and the change in these estimates, as required by Financial Accounting Standards Board No. 60, Accounting and Reporting by Insurance Enterprises, paragraph 18, is recorded in the period that the change in these estimates is made.

Page 52

Penn-America Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements - (Continued)

Note 7 Income Tax

The components of income tax expense (benefit) are as follows:

	Year ended December 31,		
(In thousands)	2001	2000	1999
	(Restated)	(Restated)	(Restated)
Current	\$ 2,492	\$(2,377)	\$ 107
Deferred	(711)	(1,096)	(586)
Total tax expense (benefit)	\$ 1,781	\$(3,473)	\$ (479)

The actual income tax rate differed from the statutory income tax rate applicable to income before income taxes as follows:

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

(In thousands)	Year ended December 31,		
	2001	2000	1999
(Restated)	(Restated)	(Restated)	
Statutory income tax rate	34.0%	(34.0)%	34.0
Tax-exempt interest and dividends received deduction	(7.7)	(10.2)	(44.5)
Other	0.2	2.4	(40.9)
	26.5%	(41.8)%	(51.4)

The tax effects of temporary differences that result in a net deferred tax asset as of December 31, are summarized as follows:

(In thousands)	2001	2000
	(Restated)	(Restated)
Assets		
Effect of discounting unpaid losses and loss adjustment expenses	\$4,490	\$4,070
Excess of tax over financial reporting of earned premium	2,502	2,625
Realized investment losses due to other-than temporary write-downs	1,241	826
Other	609	763
Total deferred assets	8,842	8,284
Liabilities		
Deferred policy acquisition costs	\$3,088	\$3,508
Net unrealized investment gain	1,600	408
Other	364	96
Total deferred liabilities	5,052	4,012
Net deferred tax asset	\$3,790	\$4,272

The Company is required to establish a valuation allowance for any portion of the deferred tax asset that management believes will not be realized. In the opinion of management, it is probable that the Company will realize the benefit of the deferred tax asset and, therefore, no such valuation allowance has been established.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Penn-America Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements - (Continued)

Note 8 Segment Information

The Company had two reportable segments: personal lines and commercial lines. These segments were managed separately because they have different customers, pricing and expense structures. The Company exited the non-standard personal automobile business in 1999 and announced that it would run-off its remaining portfolio of such business. The Company will continue to report on this segment separately until the amounts relating to the non-standard personal automobile business become immaterial to the financial statements presented. The Company does not allocate assets between segments because assets are reviewed in total by management for decision-making purposes.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies. The Company evaluates segment profit based on profit or loss from operating activities. Segment profit or loss from operations is pre-tax and does not include unallocated expenses but does include investment income attributable to insurance transactions. Segment profit or loss therefore excludes income taxes, unallocated expenses and investment income attributable to equity.

The following is a summary of the Company's segment revenues, expenses and profit:

	Year ended December 31, 2002	
(In thousands)	Commercial	Personal
	(Restated)	(Restated)
Premiums earned	\$ 88,912	\$ 22
Net investment income and net realized investment loss from insurance operations	6,667	--
Total segment revenues	95,579	22
Segment losses and loss adjustment expenses	62,414	(1,493)
Segment expenses	26,087	8
Total segment expenses	88,501	(1,485)
Segment profit	\$ 7,078	\$ 1,507

Plus unallocated items:

Net investment income from equity

Unallocated expenses

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Income tax expense

Net income

Page 54

Penn-America Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements - (Continued)

(In thousands)	Year ended December 31,	
	Commercial	Personal
	(Restated)	(Restated)
Premiums earned	\$ 87,556	\$ 3,893
Net investment income and net realized investment loss from insurance operations	3,801	353
Total segment revenues	91,357	4,246
Segment losses and loss adjustment expenses	72,893	2,485
Segment expenses	25,614	1,362
Total segment expenses	98,507	3,847
Segment profit (loss)	(\$ 7,150)	\$ 399
Plus unallocated items:		
Net investment income from equity		
Unallocated expenses		
Income tax benefit		
Net loss		

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

(In thousands)	Year ended December 31,	
	Commercial (Restated)	Personal (Restated)
Premiums earned	\$ 71,731	\$ 13,946
Net investment income and net realized investment gain from insurance operations	3,917	662
Total segment revenues	75,648	14,608
Segment losses and loss adjustment expenses	49,744	13,443
Segment expenses	21,905	4,533
Total segment expenses	71,649	17,976
Segment profit (loss)	\$ 3,999	\$ (3,368)
Plus unallocated items:		
Net investment income from equity		
Unallocated Expenses		
Income tax benefit		
Net income		

Total segment revenues of \$95,601,000, \$95,603,000 and \$90,256,000, plus unallocated net investment income from equity of \$3,494,000, \$3,492,000 and \$4,848,000, equals total Company revenues of \$99,095,000, \$99,095,000 and \$95,104,000 for the years ended December 31, 2001, 2000, and 1999, respectively.

In 2001, the Company had one general agency that accounted for approximately 11% of gross premiums earned. In 2000 and 1999, no general agent accounted for more than 10% of gross premiums earned.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Note 9 Dividends from Subsidiaries and Statutory Information

Penn-America and Penn-Star are highly regulated by the state in which they are incorporated and the states in which they do business. Such regulations, among other things, limit the amount of dividends, impose restrictions on the amount and types of investments and regulate rates insurers may charge for various products.

A source of cash for the payment of common stock dividends to PAGI's stockholders is dividends from Penn-America. Penn-America is required by law to maintain a certain minimum surplus on a statutory basis and is subject to risk-based capital requirements and regulations under which payment of a dividend from statutory surplus may require prior approval of the Pennsylvania regulatory authorities. In 2001, the Company paid dividends of \$1.6 million to PAGI. No ordinary dividends were paid in 2000. In 2000, the Penn-America paid a \$6.4 million return of capital to PAGI, after receiving approval from the Pennsylvania Insurance Department. The maximum dividend that may be paid by Penn-America to PAGI without prior approval of regulatory authorities in 2002 is \$6,473,325.

The National Association of Insurance Commissioners ("NAIC") has developed Property and Casualty Risk-Based Capital ("RBC") standards that relate an insurer's reported statutory surplus to the risks inherent to overall operations. The RBC formula uses the statutory annual statement to calculate the minimum indicated capital level to support asset risk and underwriting risk. The NAIC model law calls for various levels of regulatory action based on the magnitude of an indicated RBC capital deficiency, if any. The Company regularly monitors capital requirements along with the NAIC's RBC developments. The Company has determined that its capital levels are in excess of the minimum capital requirements for all RBC action levels and that its capital levels are sufficient to support the level of risk inherent in its operations.

The following tables reconcile statutory surplus and net income (loss) of the Company as determined in accordance with accounting procedures prescribed by the insurance regulatory authorities to stockholders' equity and net income (loss) of the Company calculated in accordance with accounting principles generally accepted in the United States as reported herein:

(In thousands)	Year ended December 31,		
	2001	2000	1999
Statutory surplus as regards to policyholders	\$ 64,733	\$ 55,530	\$ 69,515
Deferred policy acquisition costs	9,083	10,317	9,306
Deferred income taxes	(574)	4,272	5,483
Net unrealized investment gain (loss)	4,151	1,974	(5,027)
Non-admitted assets	2,171	1,175	896
Provision for uncollectible accounts	(1,022)	(522)	(522)
Holding company assets	1,594	1,156	938
Other, net	255	149	29
GAAP stockholders' equity	\$ 80,391	\$ 74,051	\$ 80,618

Penn-America Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements - (Continued)

(In thousands)	Year ended December 31,		
	2001	2000	(Re
	(Restated)	(Restated)	
Statutory net income (loss)	\$ 6,827	\$ (5,020)	\$ 1
Deferred policy acquisition costs	(1,268)	1,010	
Deferred income tax	499	594	
Allowance for uncollectible accounts	(500)	--	
Holding company expenses, net of tax	(345)	(500)	
GAAP restatement - other than temporary impairment (1)	(411)	(975)	
Other, net	138	60	
GAAP net income (loss)	\$ 4,940	\$ (4,831)	\$ 1

The NAIC revised the Statutory Accounting Practices and Procedures Manual in a process referred to as Codification. The objective of Codification is to standardize the accounting practices prescribed by each State's Insurance Department. The revised manual was effective January 1, 2001. Pennsylvania, the domiciliary state for Penn-America and Penn-Star, has adopted the provisions for the revised manual. The revised manual has changed, to some extent, prescribed statutory accounting practices and has resulted in changes to the accounting practices that Penn-America and Penn-Star use to prepare their statutory-basis financial statements. These changes resulted in an increase in the statutory-basis capital and surplus of the Company of \$3.3 million at January 1, 2001.

Note 10 Incentive Savings and Retirement Plan

Penn-America participates in a profit-sharing and a 401(k) plan with Penn Independent that covers qualified employees. Penn-America's contributions under the 401(k) plan were \$117,000, \$72,000 and \$105,000 for 2001, 2000, and 1999, respectively. There were no profit-sharing distributions in 2001, 2000, and 1999.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Note 11 Stock Incentive Plans

Stock options: In August 1993, the Company adopted a Stock Incentive Plan (the "Plan"), which was later amended and restated in April of 1994 and amended in April 2000. The purpose of the Plan is to enable officers, employees, directors, consultants, advisors and service providers of the Company and its affiliates (as defined in the Plan) to participate in the Company's future and to enable the Company to attract and retain these persons by offering them proprietary interests in the Company. The Plan authorized the issuance of up to 1,237,500 shares of common stock pursuant to the exercise of stock options or the award of restricted stock. Options are exercisable according to the various terms under which they were granted varying from one year to ten years after the date of grant. All options are subject in general to earlier termination if the optionee leaves the employ of the Company.

....

The fair value of options is estimated on the grant date using the Black-Scholes option pricing model. The model assumes the following for 2001, 2000, and 1999, respectively: expected annual dividend rates of 2.0%, 2.8% and 1.9%; risk-free interest rates of 2.0% for 2001 and 6.0% for 2000 and 1999; weighted-average expected life of the options of 4.8 years for 2001 and 2.5 years for 2000 and 1999; and expected stock price volatility of 22% for 2001 and 30% for 2000 and 1999.

Page 57

Penn-America Group, Inc. and Subsidiaries Notes to Consolidated Financial Statements - (Continued)

The Company has elected to account for these stock options in accordance with the provisions of Accounting Principles Board Opinion ("APB") #25, "Accounting for Stock Issued to Employees" and accordingly, no compensation expense has been recorded for such grants. Statement of Financial Accounting Standards ("SFAS") #123 "Accounting for Stock-Based Compensation," effective in 1996, would require that compensation expense be recorded for these option grants. Accounting for such options using APB 25 and SFAS 123 are both acceptable alternatives under GAAP. Had the Company elected to adopt SFAS 123, the effect on the Company's net income and per share results would have been:

(in thousands)	Year ended December 31,		
	2001	2000	1999
	(Restated)	(Restated)	(Restated)
Net income (loss):			
As reported	\$ 4,940	\$ (4,831)	\$ 1,410
Pro forma	4,914	(4,973)	1,385
Diluted net income (loss) per share:			
As reported	\$ 0.43	\$ (0.42)	\$ 0.11
Pro forma	0.43	(0.43)	0.11

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

A summary of the status of and changes in the Company's stock option plan is presented below:

	Year ended Decem	
	2001	2000
	(in thousands, except p	
Outstanding at beginning of year (average price of \$4.75, \$4.73 and \$4.65)	539	461
Granted (average price of \$5.17, \$4.96 and \$7.09 per share)	54	111
Exercised (average price of \$4.12 and \$2.95 per share)	(81)	(24)
Forfeited (average price of \$4.95 and \$10.92 per share)	(20)	(9)

Outstanding at end of year (average price of \$4.87, \$4.75 and \$4.73)	492	539

Options exercisable at end of year	418	442

Weighted average fair value of options granted during the year	\$ 0.81	\$1.94

Page 58

Penn-America Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements - (Continued)

The following table summarizes information about stock options outstanding at December 31, 2001:

	Options Outstanding			Options Exe
	Number Outstanding 12/31/01 (in 000's)	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Number Exercisable 12/31/01 (in 000's)
Exercise Prices				

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

\$3.60 - \$3.80	12	0.4	\$ 3.63	12
\$3.81 - \$5.07	347	2.8	\$ 4.17	323
\$5.07 - \$6.33	54	2.9	\$ 5.56	36
\$6.34 - \$7.60	45	3.4	\$ 6.79	13
\$7.61 - \$10.13	21	1.4	\$ 9.17	21
\$10.14 - \$12.67	13	2.4	\$ 12.67	13

On January 2, 2002, the Company granted 262,335 stock options to employees at an exercise price equal to the market price on the date of the grant. These stock option grants vest over a five-year period beginning January 2, 2003.

Restricted Stock: The Company has awarded shares of restricted stock to certain employees. Such shares are held by the Company and released to each grantee at the rate of 20% per year provided that the grantee is still employed by the Company or its affiliates. The Company charged \$115,000 in 2001 and \$120,000 in 2000 and 1999 to compensation expense relating to these awards. During 2001, 2000 and 1999, 15,750, 9,750 and 9,750 shares, respectively, of the restricted stock were released to the applicable employees as allowed by the provisions of the grant.

Agents' Contingent Commission Plan: The Company's Agents' Contingent Commission Plan allows its agents to receive up to 100% of their contingent profit commission awards in PAGI common stock. Agents' common stock awards for the 2000, 1999 and 1998 years, which were issued in May of 2001, 2000 and 1999, amounted to 35,189, 89,384, and 63,053 shares, respectively.

Note 12 Commitments and Contingencies

The Company's insurance subsidiaries are subject to routine legal proceedings in connection with their property and casualty business. Penn-America has been named as a defendant in litigation commenced in the Superior Court of California, County of Los Angeles, on November 6, 2000 and in an identical suit on December 18, 2000 in the County of Orange relating to our exited non-standard personal automobile business. It is not possible at this time to evaluate the probability of a favorable or unfavorable outcome, nor is it possible to estimate the amount of loss, if any. Management believes that its position is defensible as to such litigation and is of the opinion that the amount of loss, if any, will not have a material affect on the Company's financial statements. The Company is involved in no other pending or threatened legal or administrative proceedings which management believes might have a material adverse effect on the Company's financial condition or results of operations.

Page 59

Penn-America Group, Inc. and Subsidiaries Notes to Consolidated Financial Statements - (Continued)

The Company leases various computer equipment for use by its insurance subsidiaries. These leases have terms primarily expiring in less than a three-year period. Rental expenses for these operating leases were \$391,000 \$349,000 and \$392,000 for the years ended December 31, 2001, 2000 and 1999, respectively.

At December 31, 2001, the future minimum rental payments required under operating leases that have initial or remaining non-cancellable lease terms in excess of one year were \$341,000, \$150,000 and \$11,000 for 2002, 2003 and 2004,

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

respectively.

Note 13 Other Comprehensive Income

Accumulated other comprehensive income (loss) of the Company consists solely of net unrealized gains and losses. The following table illustrates the components of accumulated other comprehensive income:

(In thousands)	Year ended December 31, 2001		
	Pre-tax Amount	Tax Expense	Net of Tax Amount
	(Restated)	(Restated)	(Restated)
Unrealized gains on investments:			
Unrealized holding gains arising during period	\$ 2,328	\$ (792)	\$ 1,536
Reclassification adjustments for losses realized in net income	1,178	(400)	778
Other comprehensive income	\$ 3,506	\$ (1,192)	\$ 2,314

(In thousands)	Year ended December 31, 2000		
	Pre-tax Amount	Tax Expense	Net of Tax Amount
	(Restated)	(Restated)	(Restated)
Unrealized gains on investments:			
Unrealized holding gains arising during period	\$ 3,992	\$ (1,357)	\$ 2,635
Reclassification adjustments for losses realized in net income	2,808	(955)	1,853
Other comprehensive income	\$ 6,800	\$ (2,312)	\$ 4,488

(In thousands)	Year ended December 31, 1999		
	Pre-tax Amount	Tax Expense	Net of Tax Amount
	(Restated)	(Restated)	(Restated)
Unrealized losses on investments:			
Unrealized holding losses arising during period	\$ (9,822)	\$ 3,340	\$ (6,482)
Reclassification adjustments for losses realized in net income	110	(38)	72
Other comprehensive loss	\$ (9,712)	\$ 3,302	\$ (6,410)

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Penn-America Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements - (Continued)

Note 14 Unaudited Quarterly Financial Information

				2001
(In thousands except per share data)	First	Second	Third	Fourth
Revenues	\$ 25,994	\$ 24,687	\$ 23,837	\$ 23,837
Net income	967	994	1,551	1,551
Net income per share:				
Basic	0.09	0.09	0.14	0.14
Diluted	0.08	0.09	0.13	0.13
				2000
(In thousands except per share data)	First	Second	Third	Fourth
Revenues	\$ 23,933	\$ 24,923	\$ 24,971	\$ 24,971
Net income (loss)	1,583	(662)	(5,078)	(5,078)
Net income per share:				
Basic	0.13	(0.06)	(0.45)	(0.45)
Diluted	0.13	(0.06)	(0.45)	(0.45)

Note 15--Subsequent Event

On April 11, 2002, the Company announced a three-for-two stock split to be effected in the form of a 50% Stock dividend payable to shareholders of record as of April 25, 2002. The distribution date was May 9, 2002. The number of shares of common stock issued and outstanding and shares of treasury stock in the stockholders' equity section of the consolidated balance sheet have been adjusted to reflect the effect of the stock split. The balances for common stock and additional paid-in capital have been adjusted to reflect the effect of the stock split. The basic and diluted net income per share and basic and diluted weighted average shares outstanding on the consolidated statement of operations have been adjusted to reflect the effect of the stock split. The cash dividend paid per share and the balances of common stock and additional paid-in capital on the consolidated statement of stockholders' equity have been adjusted to reflect the effect of the stock split. The per share information in notes 2, 11 and 14 have been adjusted to reflect the effect of the stock split.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

FINANCIAL DISCLOSURE

None.

Page 61

PART III

ITEM 10. Directors and Executive Officers of the registrant

The Director's information will be in the Company's definitive Proxy Statement with respect to the Company's 2002 Annual Meeting of Shareholders, to be filed with the Securities and Exchange Commission within 120 days following the end of the Company's fiscal year, and is hereby incorporated by reference thereto.

Executive Officers of the Registrant as of March 15, 2002 are as follows:

Irvin Saltzman	79	Chairman of the Board of Directors of PAGI and Penn-America
Jon S. Saltzman	44	President and Chief Executive Officer of PAGI and Penn-America
Joseph F. Morris	47	Senior Vice President, Chief Financial Officer and Treasurer of PAGI and Penn-America
Garland P. Pezzuolo	37	Vice President, Secretary and General Counsel of PAGI and Penn-America

ITEM 11. EXECUTIVE COMPENSATION

This information will be contained in the Company's definitive Proxy Statement with respect to the Company's 2002 Annual Meeting of Shareholders, to be filed with the Securities and Exchange Commission within 120 days following the end of the Company's fiscal year, and is hereby incorporated by reference thereto.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

This information will be contained in the Company's definitive Proxy Statement with respect to the Company's 2002 Annual Meeting of Shareholders, to be filed with the Securities and Exchange Commission within 120 days following the end of the Company's fiscal year, and is hereby incorporated by reference thereto.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

This information will be contained in the Company's definitive Proxy Statement with respect to the Company's 2002 Annual Meeting of Shareholders, to be filed with the Securities and Exchange Commission within 120 days following the end of the Company's fiscal year, and is hereby incorporated by reference thereto.

ITEM 14. CONTROLS AND PROCEDURES

As of December 31, 2001, an evaluation was performed under the supervision and with the participation of the Company's management, including the President and CEO and Senior Vice President, CFO and Treasurer, of the effectiveness of the

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

design and operation of the Company's disclosure controls and procedures. Based on that evaluation, the Company's management, including the President and CEO and Senior Vice President, CFO and Treasurer, concluded that the Company's disclosure controls and procedures were effective as of December 31, 2001. There have been no significant changes in the Company's internal controls or in other factors that could significantly affect internal controls subsequent to December 31, 2001.

Page 62

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

a.) The following consolidated financial statements, financial statement schedules and exhibits are filed as part of this report:

1. Consolidated Financial Statements (Restated)

Consolidated Balance Sheets at December 31, 2001 and 2000
Consolidated Statements of Operations for the years ended December 31, 2001, 2000,
Consolidated Statements of Stockholders' Equity for the years ended December 31,
and 1999.
Consolidated Statements of Cash Flows for the years ended December 31, 2001, 2000,
Notes to Consolidated Financial Statements
Independent Auditors' Report for the years 2001, 2000 and 1999

The following consolidated financial statement schedules for the years 2001, 2000, and 1999 are submitted herewith:

2. Financial Statement Schedules.

Schedule I. Summary of Investments - Other Than Investments in Related Parties
Schedule II. Condensed Financial Information of Parent Company
Schedule III. Supplementary Insurance Information
Schedule IV. Reinsurance
Schedule VI. Supplemental Insurance Information Concerning Property and Casualty
Operations
Independent Auditors' Consent and Report on Schedules (filed as Exhibit 23)

All other schedules are omitted because they are not applicable or the required information is included in the financial statements or notes thereto.

3. Exhibit Index: 64-70

Exhibit Index

Exhibit No.	Description
3.1	Articles of Incorporation of the Registrant, incorporated by reference to Exhibit 3.1 to the Registrant's Registration Statement on Form S-1 (No. 33-66892) filed with the Securities and Exchange Commission on August 2, 1993.
3.2	Bylaws of the Registrant, incorporated by reference to Exhibit 3.2 to the Registrant's Registration Statement on Form S-1 (No. 33-66892) filed with the Securities and Exchange Commission on August 2, 1993.
10.3	1993 Casualty Excess of Loss Reinsurance Agreement with National Reinsurance Corporation, incorporated by reference to Exhibit 10.3 to the Registrant's Registration Statement on Form S-1 (No. 33-66892) and filed with the Securities and Exchange Commission on August 2, 1993.
10.3(i)	Endorsements Nos. 4 through 6 (Termination Endorsement) to 1993 Casualty Excess of Loss Reinsurance Agreement with National Reinsurance Corporation, filed with the Securities and Exchange Commission with Registrant's Report on Form S-2 Amendment No. 1 (No. 333-91362) on September 6, 2002.
10.7	Agreement dated August 20, 1993, between Penn Independent Corporation ("Penn Independent") and the Registrant regarding the reimbursement of certain employment costs, incorporated by reference to Exhibit 10.7 to Amendment No. 1 to the Registrant's Registration Statement on Form S-1 (No. 33-66892) and filed with the Securities and Exchange Commission on August 26, 1993.
10.7(i)	Amendment effective January 1, 1995 to August 20, 1993 Agreement between Penn Independent and Registrant regarding the sharing of certain operating costs, filed with Registrant's Report on Form 10-K for the period ended December 31, 1995, which has been filed with the Securities and Exchange Commission.
10.7(ii)	Amendments dated January 1, 1996, and March 1, 1996, to August 20, 1993 Agreement between Penn Independent and Registrant regarding the sharing of certain operating costs, filed with Registrant's Report on Form 10-K for the period ended December 31, 1996, which has been filed with the Securities and Exchange Commission.
10.7(iii)	Amendment dated March 1, 1997, to August 20, 1993 Agreement between Penn Independent and Registrant regarding the sharing of certain operating costs, filed with Registrant's Report on Form 10-K for the period ended December 31, 1997, which has been filed with the Securities and Exchange Commission.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

- 10.7(iv) Amendment dated January 1, 1999, to August 20, 1993 Agreement between Penn Independent and Registrant regarding the sharing of certain operating costs, filed with the Registrant's Report on Form 10-K for the period ended December 31, 1998, which has been filed with the Securities and Exchange Commission.

Page 64

Exhibit No.	Description
10.7(v)	Amendment dated January 1, 2000, to August 20, 1993 Agreement between Penn Independent and Registrant regarding the sharing of certain operating costs, filed with Registrant's Report on Form 10-K for the period ended December 31, 1999, which has been filed with the Securities and Exchange Commission.
10.7(vi)	Amendment dated July 1, 2000, to August 20, 1993 Agreement between Penn Independent and Registrant regarding the sharing of certain operating costs, filed with Registrant's Report on Form 10-K for the period ended December 31, 2000, which has been filed with the Securities and Exchange Commission.
10.7(vii)	Amendment dated January 1, 2001, to August 20, 1993 Agreement between Penn Independent and Registrant regarding the sharing of certain operating costs, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.
10.9	Restated Investment Advisory Agreement effective July 1, 1990, between Penn America and Carl Domino Associates, L.P., incorporated by reference to Exhibit 10.9 to the Registrant's Registration Statement on Form S-1 (No. 33-66892) and filed with the Securities and Exchange Commission on August 2, 1993.
10.9(i)	Amended Investment Advisory Agreement effective September 1, 1997, between and among Penn-America, its subsidiary, Penn-Star and Carl Domino Associates, L.P., filed with the Registrant's Report on Form 10-K for the period ending December 31, 1997, which was filed with the Securities and Exchange Commission.
10.9(ii)	Agreement dated April 15, 1997, between and among General Re New England Asset Management, Inc., Penn-America, and its subsidiary, Penn-Star filed with the Registrant's Report on Form 10-K for the period ending December 31, 1997, which was filed with the Securities and Exchange Commission.
10.9(iii)	Investment Advisory Agreement effective February 19, 1999, between Penn-America Insurance Company and Madison Monroe, Inc., filed with Registrant's Report on Form 10-K for the period ended December 31, 1999, which has been filed with the Securities and Exchange Commission.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

- 10.9(iv) Notice of Termination effective July 1, 2000, of Investment Advisory Agreement dated September 1, 1997, between and among Penn-America Insurance Company, its subsidiary, Penn-Star Insurance Company and Carl Domino Associates, L.P., filed with Registrant's Report on Form 10-K for the period ended December 31, 2000, which has been filed with the Securities and Exchange Commission.
- 10.9(v) Amendment dated November 7, 2000, to Agreement dated April 15, 1997, between and among General Re New England Asset Management, Inc., Penn-America Insurance Company, and its subsidiary, Penn-Star, filed with Registrant's Report on Form 10-K for the period ended December 31, 2000, which has been filed with the Securities and Exchange Commission.

Page 65

Exhibit No.	Description
10.9(vi)	Amendment dated August 2, 2000, to Investment Management Agreement dated February 25, 1999, between Penn-America Insurance Company and Madison Monroe, Inc., filed with Registrant's Report on Form 10-K for the period ended December 31, 2000, which has been filed with the Securities and Exchange Commission.
10.9(vii)	Notice of Termination dated November 2, 2000, of Investment Management Agreement dated February 25, 1999, between Penn-America Insurance Company and Madison Monroe, Inc., filed with Registrant's Report on Form 10-K for the period ended December 31, 2000, which has been filed with the Securities and Exchange Commission.
10.10	1993 Stock Incentive Plan, incorporated by reference to Exhibit 10.10 to Amendment No. 4 to the Registrant's Registration Statement on Form S-1 (No. 33-66892) and filed with the Securities and Exchange Commission on September 29, 1993.
10.10(i)	Penn-America Group, Inc. 1993 Stock Incentive Plan, as amended and restated April 4, 1994, incorporated by reference to Exhibit 4.1 to the Registrant's Registration Statement on Form S-8 (No. 33-82728) and filed with the Securities and Exchange Commission on August 11, 1994.
10.10(ii)	Employee Bonus Plan dated January 1, 2000, filed with Registrant's Report on Form 10-K for the period ended December 31, 1999, which has been filed with the Securities and Exchange Commission.
10.10(iii)	Amendment dated April 1, 2000, to Penn-America Group, Inc. 1993 Stock Incentive Plan, as amended and restated April 4, 1994, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

- 10.11 Lease effective July 1, 2000, between Penn-America Insurance Company and Irvin Saltzman, filed with Registrant's Report on Form 10-K for the period ended December 31, 2000, which has been filed with the Securities and Exchange Commission.
- 10.14 1995 Multiple Line Excess of Loss (Casualty and Property) Reinsurance Agreement with National Reinsurance Corporation, effective as of January 1, 1995, filed with Registrant's Report on Form S-2 Amendment No. 1 (No. 333-91362) with the Securities and Exchange Commission on September 6, 2002.
- 10.14(i) Endorsement No. 1 to Multiple Line Excess of Loss Reinsurance Agreement with National Reinsurance Corporation, effective as of January 1, 1995, filed with Registrant's Report on Form S-2 Amendment No. 1 (No. 333-91362) with the Securities and Exchange Commission on September 6, 2002.
- 10.14(ii) Endorsement No. 2 to Multiple Line Excess of Loss Reinsurance Agreement with National Reinsurance Corporation, effective as of January 1, 1995, filed with Registrant's Report on Form S-2 Amendment No. 1 (No. 333-91362) with the Securities and Exchange Commission on September 6, 2002.

Page 66

Exhibit No.	Description
10.14(iii)	1996 Property & Liability Reinsurance Agreement with General Re Corporation effective May 1, 1996, filed with Registrant's Report on Form S-2 Amendment No. 1 (No. 333-91362) with the Securities and Exchange Commission on September 6, 2002.
10.14(iv)	Property Catastrophe Excess of Loss Reinsurance Program between subscribing reinsurers and Penn-America and Penn-Star Insurance Companies effective January 1, 2000, to January 1, 2002, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.
10.16	Penn-America Group, Inc. 1995 Key Employee Incentive Compensation Plan, incorporated as Part I to Registrant's Registration Statement on Form S-8 (No. 333-00050) and filed with the Securities and Exchange Commission on January 4, 1996.
10.16(i)	Penn-America Insurance Company 2001 Key Employee Incentive Compensation Plan, effective January 1, 2001, filed with Registrant's Report on Form 10-K for the period ended December 31, 2000, which has been filed with the Securities and Exchange Commission.
10.17	Penn-America Insurance Company's Agency Award and Profit Sharing Plan, incorporated as Exhibit 4 to Registrant's Registration Statement on Form S-3 (No. 333-00046) and

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

filed with the Securities and Exchange Commission on January 4, 1996.

- 10.17(i) Penn-America Insurance Company's Agency Award and Profit Sharing Plan, attached as Exhibit 4 to Registrant's Registration Statement on Form S-3 (No. 333-49055) and filed with the Securities and Exchange Commission on March 31, 1998.
- 10.17(ii) Amended General Agency Profit Sharing Addendum to Agency Award & Profit Sharing Plan, filed with Registrant's Report on Form 10-K for the period ended December 31, 1999, which has been filed with the Securities and Exchange Commission.
- 10.17(iii) General Agent Contingent Profit Commission Addendum between agents and Penn-America and Penn-Star Insurance Companies effective January 1, 2001, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.
- 10.18 Stipulation of Termination of Property and Liability Reinsurance Agreement with National Reinsurance Corporation effective May 1, 1996, filed with Registrant's Report on Form S-2 Amendment No. 1 (No. 333-91362) with the Securities and Exchange Commission on September 6, 2002.
- 10.19 Multiple Line Excess of Loss Agreement of Reinsurance including Endorsement No. 1 between General Reinsurance Corporation and Penn-America and Penn-Star Insurance Companies effective January 1, 2000, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.

Page 67

Exhibit No.	Description
10.19(i)	Endorsement No. 2 to the Multiple Line Excess of Loss Agreement of Reinsurance including Endorsement No. 1 (Exhibit 10.19) between General Reinsurance Corporation and Penn-America and Penn-Star Insurance Companies, effective September 1, 2001, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.
10.20	Property and Casualty Excess of Loss Reinsurance Agreement between American Re-Insurance Company and Penn-America and Penn-Star Insurance Companies effective September 1, 2001, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

- 11 Statement re: computation of per share earnings, incorporated by reference from Note 2 to the Consolidated Financial Statements, filed with Registrant's Report on Form 10-K/A for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.
- 21 As of December 31, 2001, the Registrant's only subsidiary is Penn-America Insurance Company, a Pennsylvania Corporation.
- 28.2 Credit Agreement among Registrant, Certain Lenders and First Union National Bank dated September 28, 1998, filed with the Securities and Exchange Commission, filed with the Registrant's Report on Form 10-K for the period ended December 31, 1998, which has been filed with the Securities and Exchange Commission.
- 28.3 First Amendment to Credit Agreement, dated May 12, 1999, among registrant, certain lenders and First Union National Bank, dated September 28, 1998, filed with Registrant's Report on Form 10-K for the period ended December 31, 1999, which has been filed with the Securities and Exchange Commission.
- 28.4 Second Amendment to Credit Agreement, dated August 26, 1999, among registrant, certain lenders and First Union National Bank, dated September 28, 1998, filed with Registrant's Report on Form 10-K for the period ended December 31, 1999, which has been filed with the Securities and Exchange Commission.
- 28.5 Third Amendment to Credit Agreement, dated March 15, 2000, among registrant, certain lenders and First Union National Bank, dated September 28, 1998, filed with Registrant's Report on Form 10-K for the period ended December 31, 1999, which has been filed with the Securities and Exchange Commission.
- 28.6 Notice of Termination of Credit Agreement, dated July 31, 2000, among Registrant, Certain Lenders, and First Union National Bank, parties to the Credit Agreement dated September 28, 1998, filed with the Registrant's Report on Form 10-K for the period ended December 31, 2000, which has been filed with the Securities and Exchange Commission.

Page 68

Exhibit No.	Description
30.0	Reinsurance Pooling Agreement between Penn-America Insurance Company and Penn- Star Insurance Company dated July 1, 1998, filed with the Securities and Exchange Commission.
31.0	Amended and Restated Promissory Note and Security Agreement effective January 2, 2001, between Jon S.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Saltzman and Penn-America Insurance Company which amends and restates in its entirety, including any amendments thereto, the Promissory Note and Security Agreement dated January 17, 2000, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.

- 31.0(i) Amended and Restated Promissory Note and Security Agreement effective January 2, 2001, between Jon S. Saltzman and Penn-America Insurance Company which amends and restates in its entirety, including any amendments thereto, the Promissory Note and Security Agreement dated March 10, 2000, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.
- 31.0(ii) Amended and Restated Promissory Note and Security Agreement effective January 2, 2001, between Jon S. Saltzman and Penn-America Insurance Company which amends and restates in its entirety, including any amendments thereto, the Promissory Note and Security Agreement dated September 19, 2000, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.
- 31.0(iii) Amended and Restated Promissory Note and Security Agreement effective January 2, 2001, between J. Ransley Lennon and Penn-America Insurance Company which amends and restates in its entirety, including any amendments thereto, the Promissory Note and Security Agreement dated February 16, 2000, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.
- 31.0(iv) Amended and Restated Promissory Note and Security Agreement effective January 2, 2001, between Garland P. Pezzuolo and Penn-America Insurance Company which amends and restates in its entirety, including any amendments thereto, the Promissory Note and Security Agreement dated February 11, 2000, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.
- 31.0(v) Promissory Note and Security Agreement effective March 9, 2001, between Joseph F. Morris and Penn-America Insurance Company, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

- 31.0(vi) Promissory Note and Security Agreement effective March 28, 2001, between Joseph F. Morris and Penn-America Insurance Company, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.
- 31.0(vii) Promissory Note and Security Agreement effective March 9, 2001, between Garland P. Pezzuolo and Penn-America Insurance Company, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.
- 31.0(viii) Promissory Note and Security Agreement effective February 16, 2001, between Thomas P. Bowie and Penn-America Insurance Company, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.
- 31.0(ix) Promissory Note and Security Agreement effective February 23, 2001, between Thomas P. Bowie and Penn-America Insurance Company, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.
- 31.0(x) Promissory Note and Security Agreement effective February 27, 2001, between Thomas P. Bowie and Penn-America Insurance Company, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.
- 31.0(xi) Promissory Note and Security Agreement effective March 21, 2001, between Thomas P. Bowie and Penn-America Insurance Company, filed with Registrant's Report on Form 10-K for the period ended December 31, 2001, which has been filed with the Securities and Exchange Commission.

(b)

- (1) Form 8-K dated November 14, 2001 re: Quarterly Statements of Penn-America Insurance Company and Penn-Star Insurance Company, which was filed with the Securities and Exchange Commission.
- (2) Form 8-K dated December 4, 2001, re: delivering a presentation including a slide show to interested parties outlining the Company's business strategies and an overview of the Company's historical and financial results, which was filed with the Securities and Exchange Commission.

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

PENN-AMERICA GROUP, INC.

Schedule I - Summary of Investments - Other than Investments in Related Parties
(in thousands)

	December 31, 2001		
	Amortized Cost	Fair Value	Amount sho on Balance S
	(Restated)		
Fixed maturities Available for sale			
U.S. Treasury securities and obligations of U.S. government agencies	\$ 4,013	\$ 4,195	\$ 4,195
Corporate securities	49,981	52,021	52,021
Mortgage-backed securities	26,483	27,316	27,316
Other structured securities	20,758	21,462	21,462
Municipal securities	20,569	21,004	21,004
Public utilities	9,172	9,255	9,255
Total available for sale	130,976	135,253	135,253
Held to maturity			
U.S. Treasury securities and obligations of U.S. government agencies	13,812	14,025	13,812
Corporate securities	276	290	276
Public utilities	996	1,002	996
Total held to maturity	15,084	15,317	15,084
Total fixed-maturity securities	146,060	150,570	150,337
Equity securities:			
Common stock	7,814	7,977	7,977
Preferred stock	16,906	17,172	17,172
Total equity securities	24,720	25,149	25,149
Total investments	\$170,780	\$175,719	\$175,486

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

PENN-AMERICA GROUP, INC.
 Schedule II--Condensed Financial Information of Parent Company
 Condensed Balance Sheets
 (in thousands except share data)

	December
	2001
	(Restated)
ASSETS	
Cash	\$ 1,261
Investment in subsidiary, equity method	79,425
Other assets	359
Total assets	\$ 81,045
LIABILITIES AND STOCKHOLDERS' EQUITY	
Liabilities:	
Accounts payable and accrued expenses	\$ 25
Total liabilities	25
Stockholders' equity:	
Preferred stock, \$.01 par value; authorized 2,000,000 shares; none issued	
Common stock, \$.01 par value; authorized 20,000,000 in 2001 and 2000; issued 2001, 15,228,351 and 2000, 15,114,038 shares; outstanding 2001, 11,478,351 and 2000, 11,364,038 (1)	152
Additional paid-in capital (1)	70,735
Accumulated other comprehensive loss, net	3,106
Treasury stock 3,750,000 shares at cost (1)	(24,161)
Retained earnings	31,320
Unearned compensation from restricted stock awards	(132)
Total stockholders' equity	81,020
Total liabilities and stockholders' equity	\$ 81,045

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

PENN-AMERICA GROUP, INC.
 Schedule II--Condensed Financial Information of Parent Company
 Condensed Statements of Operations
 (in thousands except per share data)

	Years ended Decem	
	2001	2000
	(Restated)	(Restated)
Revenue:		
Dividend income	\$1,600	\$ -
Other income	26	27
Operating expenses	(548)	(791)
Income before income tax and undistributed net income (loss) of subsidiary	1,078	(764)
Income tax benefit	177	260
Income before equity in undistributed net income of subsidiary	1,255	(504)
Equity in undistributed net income (loss) of subsidiary	3,685	(4,327)
Net income (loss)	\$4,940	(\$4,831)
Net income (loss) per share		
Basic	\$0.43	(\$0.42)
Diluted	\$0.43	(\$0.42)

NOTE: Certain prior year amounts have been reclassified to conform to the 2001 presentation.

PENN-AMERICA GROUP, INC.
 Schedule II - Condensed Financial Information of Parent Company
 Condensed Statements of Cash Flows
 (in thousands)

	2001	2000
Years ended Decem		

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

	(Restated)	(Rest)
Cash flows from operating activities:		
Net income (loss)	\$ 4,940	\$ (
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Return of capital from subsidiary	--	
Equity in undistributed net (income) loss of subsidiary	(3,685)	
Amortization/depreciation	86	
Increase (decrease) in :		
Accounts payable and accrued expenses	(148)	
Other, net	74	
	-----	-----
Net cash provided by operating activities	1,267	
	-----	-----
Cash flows from investing activities:		
Change in short-term investments	-	
	-----	-----
Net cash provided by investing activities	-	
	-----	-----
Cash flows from financing activities:		
Issuance of common stock (net of expenses)	622	
Purchase of treasury stock	-	
Dividends paid to common stockholders	(1,600)	
	-----	-----
Net cash used by financing activities	(978)	
	-----	-----
Increase (decrease) in cash	289	
Cash, beginning of period	972	
	-----	-----
Cash, end of period	\$ 1,261	\$
	=====	=====

NOTE: Certain prior year amounts have been reclassified to conform to the 2001 presentation.

Page 74

PENN-AMERICA GROUP, INC.
Schedule III - Supplementary Insurance Information
Years Ended December 31, 2001, 2000 and 1999
(in thousands)

Deferred Policy Acquisition Costs	Liability for Unpaid Losses and Loss Adjustment Expenses	Unearned Premiums	Earned Premiums	Inv I
2001				

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

Commercial	\$ 9,067	\$ 117,555	\$ 40,989	\$ 88,912
Personal	16	2,043	45	22
Unallocated	-	-	-	-
Total	\$ 9,083	\$ 119,598	\$ 41,034	\$ 88,934
2000				
Commercial	\$ 10,310	\$ 109,377	\$ 43,218	\$ 87,556
Personal	7	5,937	21	3,893
Unallocated	-	-	-	-
Total	\$ 10,317	\$ 115,314	\$ 43,239	\$ 91,449
1999				
Commercial	\$ 8,914	\$ 82,192	\$ 35,188	\$ 71,731
Personal	392	11,527	1,144	13,946
Unallocated	-	-	-	-
Total	\$ 9,306	\$ 93,719	\$ 36,332	\$ 85,677

	Amortization of Deferred Policy Acquisition Costs	Other Underwriting Expenses	Net Premiums Written
2001			
Commercial	\$ 22,707	\$ 3,380	\$ 87,121
Personal	8	-	2
Unallocated	-	5,358	-
Total	\$ 22,715	\$ 8,738	\$ 87,123
2000			
Commercial	\$ 23,857	\$ 1,757	\$ 94,481
Personal	1,362	1,362	2,769
Unallocated	-	5,045	-
Total	\$ 25,219	\$ 6,802	\$ 97,250
1999			
Commercial	\$ 20,269	\$ 1,596	\$ 75,574
Personal	4,533	-	11,462
Unallocated	-	4,443	-
Total	\$ 24,802	\$ 6,039	\$ 87,036

PENN-AMERICA GROUP, INC.
 Schedule IV - Reinsurance
 Years Ended December 31, 2001, 2000 and 1999
 (in thousands)

Property and Liability Insurance Premiums	Direct	Ceded to Other Companies	Assumed from Other Companies	Net Premium Written	Perco of A t
	-----	-----	-----	-----	-----
2001	\$98,328 =====	\$11,289 =====	\$84 =====	\$87,123 =====	=====
2000	\$108,622 =====	\$12,540 =====	\$ 1,169 =====	\$ 97,250 =====	=====
1999	\$ 94,967 =====	\$ 8,947 =====	\$ 1,016 =====	\$ 87,036 =====	=====

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

PENN-AMERICA GROUP, INC.
 Schedule VI- Supplemental Insurance Information Concerning
 Property and Casualty Operations
 Years Ended December 31, 2001, 2000 and 1999
 (in thousands)

Years Ended	Liability for Unpaid Losses and Loss	Discount If Any, Deducted	Loss and Loss Adjustment Expenses (Benefits) Incurred Related to	
	Adjustment Expenses	From Reserves	Current Year	Prior Year
December 31, 2001	\$119,598	-	\$60,885	
December 31, 2000	115,314	-	66,214	9,1
December 31, 1999	93,719	-	54,768	8,4

Page 77

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: November 12, 2002
 Penn-America Group, Inc.
 By: /s/ Jon S. Saltzman
 Jon S. Saltzman,
 President and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons on behalf of the Registrant in the capacities and on the dates indicated.

/s/ Irvin Saltzman Irvin Saltzman	Chairman of the Board of Directors and Director
/s/ Jon S. Saltzman Jon S. Saltzman	President, Chief Executive Officer and Director (Principal Executive Officer)

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

/s/ Robert A. Lear Robert A. Lear	Director
/s/ Joseph F. Morris Joseph F. Morris	Senior Vice President, Chief Financial Officer and Treasurer
/s/ Garland P. Pezzuolo Garland P. Pezzuolo	Vice President, Secretary and General Counsel
/s/ Paul Simon Paul Simon	Director
/s/ Charles Ellman Charles Ellman	Director
/s/ M. Moshe Porat M. Moshe Porat	Director
/s/ Jami Saltzman-Levy Jami Saltzman-Levy	Director
/s/ Martin Sheffield Martin Sheffield	Director
/s/ E. Anthony Saltzman E. Anthony Saltzman	Director

Page 78

CERTIFICATIONS

I, Jon S. Saltzman, certify that:

1. I have reviewed this annual report on Form 10-K/A of Penn-America Group, Inc.;
2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

- a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;
 - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and
 - c) presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
- a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officer and I have indicated in this annual report whether there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 12, 2002

/s/ Jon S. Saltzman
Jon S. Saltzman
President & CEO

Page 79

CERTIFICATIONS

I, Joseph F. Morris, certify that:

1. I have reviewed this annual report on Form 10-K/A of Penn-America Group, Inc.;
2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;
3. Based on my knowledge, the financial statements, and other financial

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:
 - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;
 - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and
 - c) presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - d) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
 - e) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officer and I have indicated in this annual report whether there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 12, 2002

/s/ Joseph F. Morris
Joseph F. Morris
Senior Vice President, CFO
and Treasurer

Page 80

CERTIFICATION OF CHIEF EXECUTIVE OFFICER

PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO

Edgar Filing: PENN AMERICA GROUP INC - Form 10-K/A

SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Penn-America Group, Inc. (the "Company") on Form 10-K/A for the period ending December 31, 2001, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Jon S. Saltzman, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. ss. 1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) and 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ Jon S. Saltzman

Jon S. Saltzman
President and Chief Executive Officer

November 12, 2002

Page 81

CERTIFICATION OF CHIEF FINANCIAL OFFICER

PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Penn-America Group, Inc. (the "Company") on Form 10-K/A for the period ending December 31, 2001, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Joseph F. Morris, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. ss. 1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) and 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ Joseph F. Morris

Joseph F. Morris
Senior Vice President, Chief Financial Officer
and Treasurer

November 12, 2002

